CITE AS
28 *Energy & Min. L. Inst.* ch. 5 (2008)

Chapter 5

Master Limited Partnerships

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Synopsis

§ 5.01. Overview.

[1] — Introduction.

A "master limited partnership" (MLP) is a domestic or foreign business entity taxable as a partnership under the Internal Revenue Code of 1986, as amended (the Code), the interests in which are readily tradeable on (a) an established securities market or (b) a secondary securities market (or the substantial equivalent of a secondary securities market).[1] MLPs are also referred to as "publicly traded partnerships" (PTPs) and throughout this article the terms will be used interchangeably.

For federal income tax purposes, the term "partnership" as used in Section 7704 of the Code is a tax concept as opposed to a state law concept. A "partnership interest" includes:

1. any interest in the capital or profits of the partnership (including the right to partnership distributions); and

1 Treas. Reg. § 1.7704-1(a) (1995).

2. any financial instrument or contract the value of which is determined in whole or in part by reference to the partnership (including the amount of partnership distributions, the value of partnership assets, or the results of partnership operations).[2]

Thus, although referred to as "partnerships" from a tax perspective, an MLP can take the form of a variety of legal entities created under state law, such as partnerships, limited liability companies and other unincorporated entities. The determinative factor is whether the applicable legal entity falls within the definition of a partnership for federal tax purposes.

In accordance with Section 7704's general rule, absent an exception, MLPs are taxed as corporations under Subchapter C of the Code.[3] This exception allows an MLP to be taxed as a partnership under Subchapter K of the Code if 90 percent or more of its gross annual income consists of "qualifying income."[4]

[2] — Structure.

MLPs are typically formed as limited partnerships under the Delaware Revised Uniform Limited Partnership Act. The general partner is a separate entity which typically owns two percent interest in the MLP and manages its day-to-day operations. The MLP can be capitalized through the sale of limited partnership interests (typically referred to as "common units") to outside investors via private and/or public offerings. The general partner interests are held by a separate entity that may or may not be a publicly traded company. Depending upon the circumstances, this entity is sometimes referred to as the MLP's "sponsor."

[3] — The 90 Percent Gross Income Requirement.

In order to qualify for partnership-type, flow-through tax treatment, a partnership with publicly traded interests must receive not less than 90

2 *Id.* § 1.7704-1(a)(2)(i).
3 I.R.C. § 7704(a) (2004).
4 *Id.* § 7704(c).