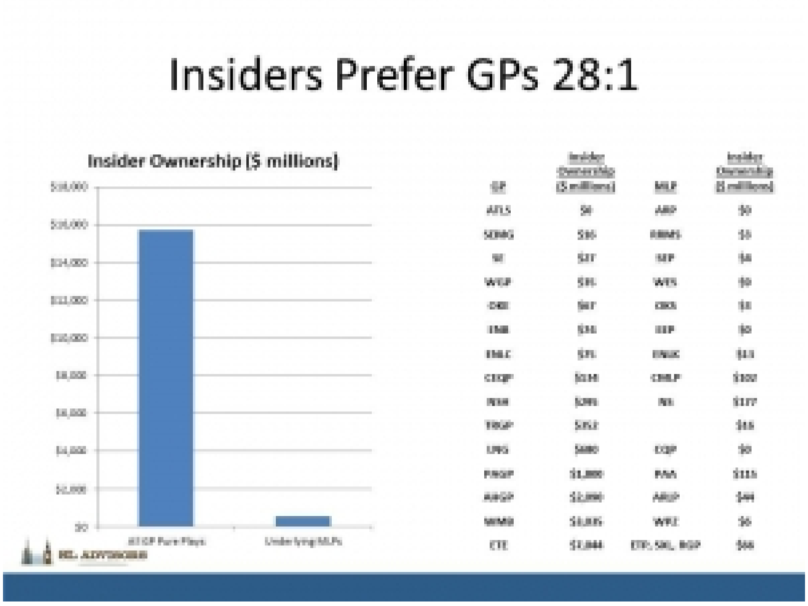
Follow the MLP Money

We’ve long advocated investing in the General Partners (GPs) of Master Limited Partnerships (MLPs) rather than the MLPs themselves. Most importantly, the GPs have preferential economics in the form of Incentive Distribution Rights (IDRs) which entitle them to up to 50% of the Distributable Cash Flow (DCF) the underlying MLP generates. This entitlement is immune



to additional issuance of equity, so GPs in effect maintain their economic stake even while the MLP grows its asset base funded with new issuance of equity and debt. In this way, MLP GPs are like hedge fund managers, in that asset growth always benefits them economically. MLP LP unitholders are similar to hedge fund investors in that asset growth may benefit them depending on the return on those additional assets.

MLP sponsors have long recognized the benefits of the GP. It’s most powerfully illustrated in the chart at left (source: SL Advisors) showing insider ownership of GPs versus the underlying MLP. By a factor of 28:1 the money invested by the people who run MLPs favors GPs over the underlying MLPs. Not every MLP has a GP. Some have bought their GP back, creating a single class of equity. But where an MLP has a GP, if you invest in it you’ll most likely be aligning your interests with the insiders. By a factor of 28:1.