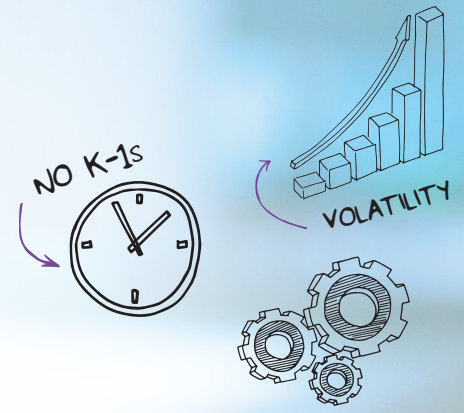


ALPS INSIGHTS

A Primer on MLP Funds



Investors have been attracted to the Master Limited Partnership (MLP) sector in recent years due to its attractive yield, low correlation to stocks and bonds and built-in inflation protection. There are multiple ways to access the MLP sector, including direct investing through individual MLPs and through MLP Funds.

This ALPS Insight provides more information on MLP Funds, including their advantages and disadvantages compared to direct investing, as well as an analysis of the factors to consider when choosing the most appropriate way to access MLPs.

MLP Investing Can be Complex

Investing in MLPs can be complicated from a tax perspective. A direct investment in individual MLPs requires K-1 tax reporting for (each individual) every single MLP that is purchased. Individual MLP investments may also generate Unrelated Business Taxable Income (UBTI), which can be problematic for qualified accounts including Individual Retirement Accounts (IRAs). Furthermore, the size of an individual MLP investment may trigger the need to file state taxes for every state in which the MLP operates. This may be cumbersome as many MLPs own extensive pipeline networks that extend across several states.

To minimize the tax complexity of direct MLP investing, investors may opt to hold a limited number of MLPs. While this strategy may reduce tax reporting requirements, it also introduces additional single-security risk.

MLP Funds Can Simplify Tax Reporting

MLP Funds simplify the tax reporting associated with an MLP investment. MLP Funds are Funds that own more than 25% of their assets in MLPs and can be organized as either Open-End Funds, Closed-End Funds or Exchange Traded Funds (ETFs).

Rather than issuing K-1s, MLP Funds issue a single Form 1099 each year and are not subject to either state tax filing requirements or UBTI. In addition, MLP Funds provide exposure to a basket of MLPs, perhaps providing better diversification than a concentrated portfolio of individual MLPs. It is also important to note that, unlike structured notes, MLP Funds retain the tax character of the underlying MLP investments. This may be an important feature, as historically a large percentage of MLP distributions have been characterized as a tax-deferred return of capital.

MLP Fund Advantages

Simplified Tax Reporting

- One Form 1099 vs. Multiple K-1s
- No State Tax Filing Requirements
- No UBTI

Diversification

Diversification does not eliminate the risk of losses.

The Impact of Corporate Taxes

In exchange for diversification, exposure and tax reporting benefits, MLP Funds are required to be taxed as corporations if their investment in MLPs exceeds 25% of the Fund's assets. This requirement applies to all MLP Funds, including Open-End Funds, Closed-End Funds and ETFs.

As a corporate taxpayer, MLP Funds are required to accrue deferred tax liabilities (DTLs) to account for corporate taxes that will be due upon sale of its securities. In a rising market, this accrual should cause an MLP Fund to trail a basket of

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