2021 AICA Tax Free and Tax Advantaged Income For Investors event Day 2 Panel #2; "Why Now May Be the Best Time to Invest in MLP/Energy Funds"

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Mike Taggart of Taggart Fund Intelligence moderates the final panel of day 2 of the 2021 AICA Tax Free and Tax Advantaged Income event; "Why Now May be the Best Time to Invest in MLP/Energy Funds". Read the transcript below to hear the discussion among Mr. Taggart and panelists Matthew Sallee from Tortoise Capital Management, and James Murchie and Sam Brothwell, both from Energy Income Partners.

Mike Taggart

Matthew Sallee

James Murchie

Sam Brothwell

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Mike Taggart: Hello everybody, my panelists are coming up on stage now. I think.

Matthew Sallee: You know I'd be the first one to figure it out.

Mike Taggart: Well, you know, while they're getting going, why don't I start? Oh, there we go. There we go, Sam's with us. And now we're waiting for one last one, I'll get started.

Thanks everybody for joining us today and staying until the end of the conference. I'm Mike Taggart, I'm the head of Taggart Fund Intelligence. I've been analyzing closed-end funds for over a decade, I've moderated dozens of panels. So hopefully that gives me some confidence that

this discussion will go smoothly. But we have a great panel here today, it's focused on energy and obviously a lot going on in the space. Prices going up, energy transition well underway pending legislation. Here to give us a clear understanding of all that are Matt Sallee, the president of Tortoise Capital Management, Jim Murchie, the founder and CEO of Energy Income Partners, and Sam Brothwell, the director of research at Energy Income.

Why don't we kick it off, Matt, could you spend a little time. Tell us please about Tortoise, your strategies, that sort of stuff.

Matthew Sallee: Sure, I'll keep it fairly brief and leave time for us to all have more of a discussion, but basically with Tortoise we are broadly focused on essential assets. Basically what we define is what a lot of people call real assets. Basically primarily we focus on energy infrastructure, which when I say energy infrastructure I'm including midstream, power, utilities, renewables, and increasingly energy technology. We grew up, when I say grew up, the firm at its inception was purely focused on MLPs, that became midstream and then eventually has evolved to energy infrastructure.

We've kind of built out our capabilities really over the last, call it 10 years. Expanding outside of midstream to add a renewable team based in London, a private team focused on SPACs or energy transition opportunities, private team focused on wind and solar, biomass, renewable natural gas, things of that sort. So really have kind of built out our capabilities over the years and today as a firm TortoiseEcofin's 130ish employees. About 30 of those are investment professionals focused on energy, public, and private, and globally. So that's kind of the quick thumbnail.

Mike Taggart: Excellent. Thanks Matt, thanks for that. Sam or Jim, I don't know which one of you wants to take this. But Jim, how about doing us the same for Energy Income, please?

James Murchie: Sure, since I'm one of the co-founders I'll also tell a story, although Sam and I know each other for coming up on 20 years now. EIP was actually formed by reverse inquiries for people that knew me and my co-founders from the energy industry, about how I was investing my capital really since the mid-90s when I was at Tiger Management where I went after I was at Sanford Bernstein. I was the energy analyst there, and before that I was at British Petroleum for eight years.

What makes EIP different is that we're there to manage our own capital and our investors are there to invest alongside of us. Having worked in the industry my whole life I kind of know where the returns are, and the returns are really where you have utility type businesses that get allowed or agreed rates of return on monopoly assets. We are indifferent as to whether the firm is formed as an MLP. We used to have income trusts in Canada, there was a bunch of closed-end funds that used to invest in those. We're indifferent as to whether the company is called a yield corporation or utility. Those names really don't describe the assets of the company, they describe in effect the liabilities of the company. How the company is financed.

And what matters to us is that the earnings are growing and stable, because that is what supports the payout of dividends. Cyclical businesses have very low payout ratios because of that. So it

matches up well with our skillset and personalities, and so we sub-advise a few of the closed-end funds advised by First Trust because we have this expertise in stable income infrastructure. As we tell our financial advisors just the way to think about us is poles and wires, and pipes and tanks. That's what keeps us out of trouble as we say with the monopoly assets.

Mike Taggart: Excellent. Well, thank you for that brief overview. Before we get into the current landscape and exactly how your funds, what the strategies are, especially in today's environment. I'd like to just take a step back and get a sense of the bigger picture. We'll start off with Matt and then Sam and Jim, you can jump in. But Matt, can you discuss the energy transition and how infrastructure companies play a crucial role in that, please? To start it off.

Matthew Sallee: Yeah, let me just start with the big picture and then can also define, or explain how we define energy transition. Just in the big picture, the world's population is growing, every day the world needs more and more energy to meet the economic growth and population growth that is most certain to come in the future. At the same time we're trying to meet those needs with a conflicting desire to have less carbon in the atmosphere. So that in a nutshell is energy transition at a high level.

Our view is the best solution to achieving or satisfying both of those goals in unison, and doing so economically is in all-the-above approach. Which basically is electrifying everything that is possible to be electrified, but then doing so with electricity that is coming from cleaner sources, specifically wind, solar, and natural gas. So really we believe in the all-the-above approach to decarbonizing the economy. There's also some emerging technologies of course like carbon and capture and hydrogen that are a little bit further out but I think certainly can help play a big part of the role. And we can dive in a little bit eventually into how energy infrastructure companies play into that.

But the other thing I wanted to add is just depending on where you live across the globe, I think energy transition can mean different things. If you're one of the two and a half billion people across the globe that don't have access to electricity or natural gas for simple things like cooking food for your family, I think energy transition can mean getting access to that electricity or getting access to natural gas so that you're not using coal, or wood, or animal dung to cook inside your home. That in the developing markets I think is a big part of energy transition.

China and India, where they're producing two thirds of their electricity from coal, or two thirds of the total energy coming from coal, energy transition can mean getting onto cleaner sources of energy. Whereas in the US people think energy transition, they think of buying a Tesla. So very different kind of definitions from my perspective in terms of energy transition depending on where you live.

Mike Taggart: Would you agree, Sam, Jim?

Sam Brothwell: Yeah, I would just make the observation that energy has been transitioning since we discovered fire. And most recently the abundance of shale here in the US has allowed our energy policy to shift, it was always the stumbling blocks of the economy. We were always trying to have energy security, energy independence, and we've achieved that. We've gone from

being an importer to an exporter, natural gas and crude oil. And if you told me that 20 years ago I would have laughed at you, but we are there. And so now our discussion about energy has turned to environmental impact.

But we've also seen along that journey that we've got to remain mindful of the importance of other performance attributes; reliability, safety. Without those you're going to undermine public support for these emergent technologies. We're seeing that happen in California right now. They've made a very aggressive push to drive all fossil fuels, and particularly now natural gas, out of their electricity mix, and that is resulting in reliability problems with the electric grid when the sun goes down and solar electricity production falls. And so you've got a situation where customers are turning to backup generators, which are often fueled by diesel, to provide their own reliability. And that just does not strike me as sound energy or environmental policy.

Bottomline is fossil fuels still make up over 80% of the primary energy sources, that's the energy that we start with. So it'll be very difficult if not impossible to decarbonize by 2050 without leveraging the technology that we already have in things like Matt mentioned, carbon capture, utilization, and storage to extend the incumbent life that that gas generation that's really providing the reliability.

Matthew Sallee: Sam, you make a good point there, if I could just add on. You're seeing it right now going on in Europe, when reliability becomes an issue you get adverse outcomes. Where all of a sudden you're trying to pull coal back into the power mix, because at the end of the day number one, the responsibility of the power company is to keep the lights on. Just to underline, you bring up such a good point with reliability.

James Murchie: One of the things, every industry loves to think that they're special, and they all have their unique characteristics but in other respects they're not. Energy is like every other industry, where market share is achieve through some combination of cost and performance advantages. Sam touched on that. And so for the energy system, besides cost, the performances are reliability, safety, and environmental impact. And when people focus on one and ignore the other, very often it's the other that comes out of left field and frustrates the objective of what they're talking about. And so one of the things that our firm does is have a lot of engagement with regulators and policy makers. And we make this point all the time, Matt referred to all of the above, which is sort of what we use in the industry as shorthand for saying, "Don't pick solutions, pick outcomes."

Solutions would be, "I want 20% of electricity from some solar and 20% from wind." Solutions are, "I want 99.99999% reliability. I want zero carbon by 2050. And I want a safety record of X, Y, Z." Those are outcomes that the industry can then invest and achieve. It's confusing for investors because they have politicians all the time pushing their particular technology, because of course there's businesses that give them campaign contributions to do just that.

And the last thing since neither Matt or Sam really spoke to your question on infrastructure, the energy system is to some degree becoming more complex. If you think about the electric system, it started off being sort of a central radial system. Think of driving into a town in the Midwest where the first thing you see is a water tower, and that tower holds water pressure behind

everybody's faucet. The water isn't sent to your faucet, the pressure is always. And so the water in effect is asked for. Electricity works the exact same way. It's a [inaudible], but as the system becomes more sophisticated and complex, that flow will be in both directions. You have that with rooftop solar for example today.

And so while we get the question all the time of the utilities being disintermediated, actually it's the opposite that is true. You cannot run a shared resource network without the connections between them. Sam makes this point all the time. Your smartphone has a million times the computing power that Neil Armstrong had on July 20th, 1969, but it's not very powerful when it's in airplane mode. And so all of the value of all these newer, cheaper, in some cases intermittent energy technologies, are weaved together with networks of natural gas pipelines, and poles, and wires so that not each consumer has to have the storage it would take for them to go through a two-month dry spell. Whether it was cloudy or lack of wind, whether they're using their own windmill or their own solar panels. Shared network is far more efficient. And history has demonstrated this over, and over, and over again no matter what industry you look at.

And so that's the question I think investors are hearing all the time from solar panel manufacturers who are frustrated because the utility doesn't hook them up. So they say, "We're going to put the utilities out of business." The opposite is true, that solar panel has no value without the utility. Because without connecting that electricity to the rest of the grid, it's an island and islands have a lot less value. Mike, you're on mute. Mike, you have to unmute yourself.

Mike Taggart: Thank you. I had some technical issue and I got booted off the internet. Thank you, Jim. Sam, do you want to pitch in on where energy infrastructure companies fit in here on the energy transition? Anything to add to what Jim just said?

Sam Brothwell: I'll speak to the utility part of it, but the investor-owned electric utilities last year 2020 invested about $140 billion in new capital projects. Power generation made up just under $40 billion of that spend, and 75% of that in terms of technology was renewable, wind, solar, storage. Another $40 billion was invested in new high-voltage transmission, which is also essential to delivering renewable wind and solar from where it's produced, which is largely in parts of the country where there aren't people, to where it's used. You have to make that connection.

Last year about 40% of US electricity came from carbon-free sources, which includes wind, and solar, hydro, and nuclear. Coal used to supply over half of our electricity in the US, that's now a little bit below 20% share and expected to continue heading lower. So I think the energy infrastructure companies, particularly the utilities, but also the pipelines and perhaps Matt could speak to that, are paying a key role in facilitating this transition. And I think natural gas in particular, I alluded to the need for reliability, I think that is a critical role that gas is playing and probably will have to continue to play for some time.

Mike Taggart: Yeah, I'm from Pittsburgh originally, and my grandmother used to have stories about how a guy would wear a white shirt once, and after that it was always grayish. You couldn't get the gray from the coal dust out of there, and now it's beautiful. Obviously

Cleveland, they've cleaned up. I have a sister in Cleveland and I like to joke with her that Cleveland's a beautiful city, the Cuyahoga hasn't caught on fire in decades. And I grew up on the Marcellus Shale, somebody mentioned that earlier. I grew up on that before we even knew what that was, but it was under my feet my whole growing up years. Anyway, that little tangent. Matt, did you want to talk about the pipelines and that sort of thing, and real assets?

Matthew Sallee: Yeah, I would just kind of emphasize a point that both Jim and Sam made, and expand on it. But basically it goes back to how do you define energy transition? I think Jim made the point ultimately, you want a solution or an outcome in terms of, "We want lower carbon but we want to keep the lights on." So how our energy infrastructure, US midstream companies playing a role? Well, think about how much energy we're exporting now. Even the oil we export is a lower carbon intensity than a lot of other parts of the world, but more so specifically on natural gas and LPGs, liquified propane gas. That's going to developing markets and displacing coal and other very carbon-intensive fuels that those parts of the world are reliant upon. In terms of defining energy transition as keeping the lights on with less carbon, that's a huge role that these companies are playing thanks to primarily US shale.

Going beyond that, as you look forward into the future, pipelines are certainly starting to take how developed markets define energy transition, take that quite seriously. We're seeing significant portions or some pretty large quantities of renewable fuels blended into existing infrastructure. And when I say renewable fuels, I'm specifically referring to renewable diesel, which is made from animal fats or other plant-based products. Or renewable natural gas, which can come from a number of sources, but primarily landfills where the methane's just bleeding off into the environment. You capture it and turn it into a valuable product rather than a source of emissions.

But also livestock waste, that's a huge source of methane in the atmosphere. You can take the wastewater coming off of a dairy farm for example, process that and make very valuable natural gas in terms of that gas can have a negative carbon intensity. So in other words you're taking more GHG, greenhouse gas equivalent out of the atmosphere than you're putting back into it by burning that gas. And the environmental attributes of that gas are extremely valuable, so you're starting to see pipeline companies get very serious about sourcing those renewable fuels into their existing pipeline infrastructure.

If you look forward a few more years, carbon capture is really starting to get a lot of attention and I think a lot of the existing energy infrastructure, including powerplants, can be retrofitted with carbon capture technology to effectively create very reliable zero-carbon electricity and basically eliminate a lot of emissions that are otherwise going into the environment from industrial processes or the energy infrastructure itself. And then if you look out even further into the future, some companies are piloting, basically taking hydrogen and blending that into the natural gas stream.

Or ultimately I think the holy grail would be completely replacing natural gas with hydrogen. Which is pretty far out in the future, but just a few different ways that energy infrastructure companies are participating in newer, low or no-carbon fuels, or even negative carbon fuels. And the total addressable markets of carbon capture I believe is about $2 trillion, these are all

estimates of course. Hydrogen's estimated to be about a trillion dollars, renewable diesel is pretty big, renewable natural gas is a fair bit smaller but the carbon intensity attributes there I think are particularly interesting in that I think you can get significantly carbon negative fuels.

James Murchie: I have one last point on the role of the utilities, whether they are a gas utility or a power utility. But in particular we're passing 10% of our electricity coming from wind and solar in this country, and the vast majority of those facilities have been built on the back of 20 to 25-year contracts that are underwritten by investor-owned municipal and cooperative utilities that have monopoly positions that are allowed to pass those costs through to their rate payers. Those 20 to 25-year contracts have cut the cost of financing of those projects by more than half.

And so while a lot of people think that those facilities compete, whether it was with natural gas or with power utilities, actually the opposite is true. Those facilities are enabled by the balance sheets and the monopoly positions of those utilities. On the gas side, something Sam and I have worked extensively on with the Environmental Defense Fund and the Federal Energy Regulatory Commission is changes to how the natural gas pipeline contracting system works. Because the system was built around demands for natural gas that were primarily seasonal in nature, what has happened in the last 15 years is natural gas used for power generation has become 40% of the natural gas shipped through these pipelines, up from 15% fifteen to 20 years ago.

With the increased intermittency of wind and solar, what that means is that the natural gas demands are intermittent themselves, increasingly backing up intermittent wind and solar. And that puts pressure on the contract structure of these pipelines. And so as investors we have been working to make sure that those contract changes are consistent with a regulatory model that keeps the cost of financing low by making those cashflows continue to be predictable. But managed in such a way that spare capacity in those pipelines is economically allocated to the people that can use it best. And so this is a very inside baseball element of the energy transition, but people forget that energy transition isn't just windmills, solar panels, and batteries, it is the existing system changing how it works.

Mike Taggart: Yeah, as if I didn't think there was enough going on with energy transition. After just that 10 minutes there, you've doubled what's going on with the energy transition. Before we leave the energy transition infrastructure segment, I wanted just to throw out there. Specifically for midstream firms, why should investors expect that the returns of such firms going forward are going to be any different than what they've received over the last five years? Does that make sense?

Matthew Sallee: It does, yeah. I can kick it off real quick I think. Sam, and Jim, and I all probably have pretty similar answers. Let's look over the last five years, and it's no secret that midstream returns have been pretty poor, certainly on a price return basis very poor. The companies in a lot of cases had poor governance, misalignment of interests between management or the sponsors, and to the limited partners, companies were spending enormous amount of capital to meet growing oil and natural gas production domestically. Those returns turned out to not be great just because they were growing at such a rapid pace. You can go down the list, but companies are certainly resistant to energy transition and being part of the climate solution.

We're slowly making improvements over the last several years, but I think 2020 and Covid certainly kind of switched everything into high gear. I'd say some of the biggest changes in my mind is the US production growth has leveled off. It's fallen from peak levels and has leveled off. And that means that midstream companies don't need to invest $50 billion per year anymore to meet the growing production of their customers. These companies are still producing a very similar amount of cashflow, they're just not reinvesting it in their business.

In some cases that cashflow's been used to reduce debt where necessary, but increasingly we're seeing that cash being returned to shareholders. Not only in the form of more stable dividends, but along with those dividends a number of companies have initiated and are acting upon buy-back programs. I think that's a big deal because when you look at the valuation that a lot of these midstream companies are trading at, just using very simplistic cashflow they're producing, what's the cashflow yield? Not the dividend yield but the cashflow yield. To the equity they're in a lot of cases mid-teens or higher. I would argue buying back shares are going to deliver basically risk-free or nearly risk-free returns equivalent to that level. I think increasingly we're seeing companies return that capital to shareholders, which is a big tailwind for the space.

Mike Taggart: Just to follow up on that cashflow comment, and maybe Jim or Sam you can answer this as well. We've got a question here, and instead of keeping it to the end it just fits perfectly right here. So why have MLP closed-end funds gone from being such great increasing income vehicles to constant dividend cuts and hence loss of capital? And is this going to turn around? If so, why do you think that?

James Murchie: I just want to pick up on what Matt said. What happened in the midstream space should be a warning to anyone who thinks they're going to get rich on renewable energy producers. The energy as a commodity business with cyclical competitive margins where reductions in cost lower prices, which means that all of the equipment you had on prior to the last technological improvement is now on economic. And [inaudible] the difference for investors between a growing topline and a growing per share bottom-line. And if I've said that once, I've said it a million times.

Investors are constantly attracted by financial headlines about what industry is growing. But all that matters is per share earnings growth, and whether that growth is stable or not, and whether or not therefore it can support dividends. And what everybody missed with the midstream space was overinvestment. And because most of those companies were held by publicly traded partnerships, then what happened was the public turned against that structure, because they were told that that structure was shorthand for stable income. Nothing could have been further from the truth, it only defined how the companies were in fact financed. It didn't tell you anything about how the companies were operating their businesses.

And so for people that think that rushing headlong into any energy source as an investment because there's a lot of topline growth, can very well get the same treatment that midstream and shale producers investors got over the last 10 years, which is their per share earnings shrank while the topline was growing. I can't say that too many times.

The closed-end fund issue is one quite frankly of leverage. The questions we got all the time was, "Are companies cutting dividends?" And when you look at the dividend history of the companies in our closed-end funds, they continue to grow all the way through. But if the market cap of the companies goes down, then the amount of leverage the fund can support goes down with it. Because your leverage metrics are marked to market of what the shares are trading for, not the income that the portfolio was throwing off.

And so what that means is, let's say you could have in theory a set of companies whose earnings are growing their dividends steadily at 5% a year. But there's a financial crisis or a pandemic or some other kind of panic where the shares fall 40%. Those closed-end funds have to then shed debt, and to do that they are selling shares that are down 40%. And so the difference between our funds and the others is we've always run a diversified, non-cyclical energy infrastructure portfolio with utilities and other things in it. And so when one group falls, those aren't the ones you sell. You sell the ones that have a higher value.

But if everything that you own is moving together, you don't have that option. And so the risk to these closed-end funds is, A, leverage, B, the volatility of the share prices, and C, yes, the actual underlying dividends matter. It's just that in our situation that performance on the dividends was quite good, but it didn't matter if the share prices are down 40%. Which is what happened during the pandemic and what happened during the Financial Crisis.

Mike Taggart: Thank you for that, Jim. I think that's the answer I would have given as well, but you said it much more concisely and elaborately than I would have. Thank you for that. When we were preparing for this panel, we'd speak about current events and legislation. Obviously they're kind of the same thing. So I'd like to move onto that, but combine them so that we have time afterwards for each of you to speak specifically, Matt about Tortoise, and Jim and Sam about Energy Income.

So current events, Sam, I'm going to throw that to you, or Jim to kick us off on that. A lot going on in terms of we see it every day with prices, oil prices, energy prices, that sort of stuff. But also now we have the infrastructure bill, and that's obviously going to have some repercussions with energy. So do you want to get us kicked off on that topic, please?

Sam Brothwell: Well, the legislative front, there are so many moving pieces. As we've seen, getting something passed is extremely hard. We had the first bipartisan effort in recent memory that got the original infrastructure bill passed. And in the Senate, it's still not law. So that shows you how hard this is. When we look at the Biden administration's goals around energy and infrastructure, it speaks to significant investment needed in all kinds of things, smart grid infrastructure, renewable power generation, electric transmission, the things that I talked about before. And so regardless of where the power is coming from, that core electric utility grid, network, whatever you want to call it, is going to be absolutely essential to making it happen.

And when you look at the utility sector and you think about some of the politics of what they're trying to achieve here, they're trying to create jobs. And if you listen to Joe Biden, it's good paying union jobs. Well, that's what the utility sector is all about. It is the largest private sector employer of union labor in the country. So there's definitely a [inaudible] jobs and the interesting

thing about the utility industry is the thing that drives earnings is investment. Investment in what we call the rate base, which is the poles, and wires, and pipes that do the work. And so anything that encourages investment in that infrastructure is going to be good for the companies that we invest in because it's going to drive earnings growth, and that kind of creates a virtuous circle of lowering the cost of capital. So I think the legislative front is certainly a net benefit to utilities and energy infrastructure companies.

On the topic, I think what's happening with natural gas prices, this issue seemed to have emerged in Europe, where they've seen sharp declines in domestic gas production. The North Sea is down 28%, that's one of their largest producers, kind of akin to one of the big shale plays here in the US. But it's getting old, so it's down 28% versus year-to-date a year ago. Other parts of continental Europe, there's a major producing field in the Netherlands that is basically shut down. And so Europe has become much more dependent on imported liquefied natural gas or LNG. Europe also depleted last winter, it was cold. So they drew down their gas inventories and have been trying to refill, but then you get to what's happened this year.

You hear about supply chain issues all the time, remember the Suez Canal blockage? Well, a good portion of the LNG trade, particularly LNG that's moving from the Middle East to the UK and other continental Europe, that moves through the Suez Canal and that was interrupted for a period of time. Then the US has become a major exporter of natural gas, LNG, and we had storms that hit the Gulf Coast and interrupted our ability somewhat to produce but certainly it shut down some of those export facilities.

So gas prices are up in Europe, why does that affect us? Well, we're no longer and island, we're a big exporter of LNG and so our market becomes linked to the global market. And to the extent prices are up in the global market, that's going to exert upward pressure for us. And I think that all speaks to putting energy on peoples' minds, and it becomes another frontpage issue, economic concern. There's talk about inflation, all these things tie into that. So I think that in terms of current events, those are two that certainly come to my mind. We'll see how things play out on the legislative front. As you know, energy is just one piece of a broader picture, everybody's got their hand out, but it's certainly a very important piece.

Mike Taggart: For sure, Matt?

Matthew Sallee: Sorry, I was just going to make one comment. It's just something I find interesting related to what Sam was talking about in terms of high gas prices in Europe. Then you get into all these derivative effects that if you're in the industry you might foresee it, but most people are not going to think about these things. But really high natural gas prices have resulted in a lot of fertilizer plants curtailing operations. Which a byproduct of producing the fertilizer is CO2, so the CO2's not available and that's impacting food packaging, food processing. So all of a sudden it's creating, not necessarily shortages in the food, but the potential for and the rising prices in food. So you have all these spiraling effects that in the end up resulting in inflation, which is just kind of fascinating to watch.

Mike Taggart: Yeah, the pandemic of course has really highlighted how interconnected everything is. And just in time. One of the questions I wanted to ask is, and Sam, you may have

touched on this, the carbon tax. How would a carbon tax affect your portfolio company, or the companies that you all invest in?

Sam Brothwell: Well, in a couple of ways honestly. I think having a price discovery mechanism for carbon would be very beneficial. Because Jim spoke to outcomes, here you just put a marker in the ground, we just put a price on. So I think about the nuclear plants that currently supply probably half of the carbon-free electricity in this country. They're struggling to compete with lower cost natural gas and renewables at the margin because nuclear plants are by their nature a high fixed cost, low variable cost technology. So we're faced with situations where some of these plants that are closing down for economic reasons, because they're not getting paid for the carbon-free electricity that they're already providing. So carbon tax clearly would be beneficial in that regard.

How would a company recover it? Well, if you're a regulated utility, it's a cost. You recover the cost of income taxes, you recover the cost of property taxes as part of your regulated tariff. So it is kind of neutral in that regard. Certainly if you think of who's going to be a loser on a carbon tax, it's going to be coal. It's the most carbon intensive fuel out there. Liquid fuels for transportation, which we haven't even talked about electric vehicles. We can perhaps come back to that, but that would be another way. If a policy aim is to stimulate adoption of electric vehicles, putting a carbon tax on, transportation's now the largest contributor to carbon emissions. The electric power sector has driven its carbon emissions down by 40% since 2005. It is the single largest contributor to the US overall reduction in carbon emissions since 2005, which are down what Jim? About 15% or so?

James Murchie: Yeah, and you have to adjust it for the pandemic, so it's 15 or 16%. Yeah, over 90% of our carbon emission reductions are from a sector that makes up less than 3% of the market cap of the S&P 500. All the other sectors are essentially emitting the same or more carbon today as they did 15-20 years ago. And so that [inaudible], Biden is saying, "Hey look, maybe we should accelerate the power system zero carbon target date to 2035." Because if you think about it, they're large plants, it's a fixed-base system, it's not 240 million cars and trucks driving around the highway, all of which have to be replaced to electric. Which is going to take forever to do.

The electric power system, while it is mostly privately owned, operates under this cost-plus model. And so you have the policy tool to be able to tell these companies what they have to do to earn their own rate of return. It really is the most powerful public-private partnership that sits at the center of the energy system. And the other thing is we don't teach civics in high school anymore, so based on the questions we get when we hear headlines that are coming out of the White House or out of Congress, it's confusing for folks to recognize that so much of this stuff is controlled at the state level. So all of the gas utilities and electric utilities are regulated at the state level.

Mike Taggart: I just want to jump in, I'm sorry but you got me on something. So as investors when you're putting a portfolio together, we hear headlines coming out of Texas, especially last winter, California, the energy grid in both states is very fragile. How does that influence which

utilities – obviously that's headline, you guys know the deeper stories – but how does that influence what states and what utilities?

James Murchie: I'm going to turn it over to Sam, and Matt if he wants, but one thing for the listeners they need to understand is that our energy system is a blend of competitive markets and regulated markets. And so about half the electricity in this country is generated by competitive producers that live and die on the margin between their raw materials and the price of electricity that they sell, just like an aluminum smelter or a refinery. The other half is part of this regulatory rate base that Sam talked about. It is part of the state regulated utilities that are running a cost-plus model.

And so in Texas, and in California, the power is generated by a competitive merchant market. When we deregulated electricity [inaudible] years ago, it was an extraordinary success from a cost standpoint. Because prior to that going back all the way to World War II and before that, power generation was part of this cost model. Costs ran out of control and it led to deregulation that part of the business. To give you an idea of the success, wholesale prices if we had a wholesale market in the early 1980s, which we didn't, but the biggest industrial customers would have paid that price, they paid six to eight cents a kilowatt hour. Adjusted for inflation, that would be 15 to 20 cents today. Today the wholesale price of electricity [inaudible].

That success however has a cloud behind the silver lining. And that is that just like a petroleum refinery or an aluminum smelter, they make their most money when supply and demand are tight. Those companies don't have an obligation to produce. But the public may not care if there's an aluminum or a copper shortage, but they care a lot if there's a power shortage because there's rolling blackouts. And so this is what economists call a market failure. The question is, how do you incentivize a free market provider of electricity to have spare capacity that doesn't get used 99.9% of the time? That is the challenge. And different regions deal with that challenge in different ways. But California and Texas are ironic in that they have two completely different approaches to regulation, but they both ended up with the same result, which is an unreliable energy system.

Mike Taggart: Before we go on I just want to make sure we know we have 13 minutes left. So I want to give Matt a chance to talk about Tortoise-specific strategies and I want to give, Jim and Sam I want to give you both an opportunity to talk about Energy Income, your strategies, your perspectives, the specific First Trust closed-end funds that you sub-advise. And then if the audience has any questions, please throw them in through Q&A so we can get through them. Sam or Matt, if you want to follow up on what Jim said very quickly, and then we'll flip over to Matt.

Matthew Sallee: Yeah, I was just going to make one. I think the bottom-line, the crux of what Jim was describing there is that in particular for the regulated utilities or just utilities in general, I think when you're selecting the securities you have to understand the regulatory environment. In particular the state that you're operating in, and that can vary very significantly. Sam's more of an expert than I am, but I'd say California's probably a difficult environment to operate in. Like Michigan or Wisconsin, very friendly. So I think to me personally that's one of the biggest factors that we would look at.

Mike Taggart: Thank you very much for that. Jim, I was always kind of curious how that worked.

James Murchie: Well, the management teams too, you can have what seems like a bad regulatory regime but it's actually management's fault because they have a bad relationship with the regulator. And so the trick in stock picking is really understanding the people that run these companies. And there are good management teams in bad jurisdictions, but there's also bad management teams in good jurisdictions, and they find a way to mess it up.

Mike Taggart: All right. Well, Matt, so we have 10 minutes, let's give you four minutes. I'll give each of you four minutes, I'm going to put you on the clock here. Tell us about Tortoise, your strategy, and how you tackle this kind of environment. And specifically if you could somehow mention TYG, that's always been an interesting fund to me, and I know you changed the investment mandate last year. Go.

Matthew Sallee: Yeah, just backing up, so as I mentioned we have 30 energy dedicated investment professionals, that includes midstream, power, renewables, both domestic and international, so we kind of see everything. And we think if you just look at broadly infrastructure as an asset class, you look at the S&P Global Infrastructure Index, about two thirds of it, very simplistically about a third is utilities and renewables, about a third is energy, it's a little less than that, and about a third is industrial or transportation infrastructure.

If you want to invest in infrastructure, we personally think that the energy side of infrastructure is the best place to be in, and in that I would include utilities, renewables, and midstream. If you were interested in decarbonizing the global economy, I think that's a really great place where there's a lot of improvement to be made. So within infrastructure we think power, utilities, renewable, midstream are a really interesting part, or the more interesting part of global infrastructure.

And specifically on TYG we're bringing all those resources to bear as we transition that portfolio which initially in its IPO in 2004 it was an MLP product. It has evolved over time to become more of a midstream, forget about the wrapper, we like good assets, good pipelines. Now the next evolution of that product is really to be more of a diversified infrastructure, in particular an energy infrastructure investment vehicle. So we announced last year that it has broadened its mandate and is transitioning from purely owning or largely purely owning midstream holdings to a blend. Very simplistically call it 50-50 between power renewables on one side of the ledger and midstream infrastructure on the other side of the ledger.

And then we're blending in a little bit of energy technology companies, and I would use that to describe whether it's electric vehicle charging, batteries, hydrogen, any number of those things. So a small allocation there as well. That portfolio in its evolution, we're very sensitive to selling midstream at very low valuations and buying things that have had better performance over the last five years, just very simplistically speaking. But that portfolio is transitioning over time to a broader energy infrastructure mandate, and that's kind of how we're expressing our views of energy transition.

Mike Taggart: That was very concise, thank you for that. And then Jim, Sam, in addition to talking about your strategies, maybe talk about how participants and people who view the replays, how can they access that as an investor? How can they access your strategies? If you can mention that as well, please.

James Murchie: Sure. So just about our firm, we're partner-owned and we're meant to be a multigenerational firm actually, another thing that makes our unique. One of our founding partners has retired, and what happens when a partner retires is their shares sunset and they go back to the pool [inaudible]. Our firm is designed to never be sold. It's like a multifamily or single family office in that regard. We go to work every day to manage our capital and make sure that it's multigenerational in its scope in terms of time.

The approach we've always taken, because I'm a generalist investor first and an energy investor second, is that we see companies with stable growing earnings per share. And our expertise is in energy, and so where we find that is what we invest in. Like I said before, we don't care whether it's an MLP, or an income trust, or an energy infrastructure REIT, or a C-corp, or a utility, or any other label that people want to put on it. What matters is that the assets and the people running those assets have a history and therefore a prognosis of stable growing earnings.

And when you look at the energy sector, that's very hard to find. You can look at the earnings trajectory over the last 20 years of the Alerian MLP Index and it is highly cyclical with no growth. It's better growth than the S&P energy sector which has been negative. It's better growth than the S&P or Global Clean Energy Index, which has an earnings level today less than half of what it was when it was started 15 years ago. And so that's what matters to us because that's what supports growing dividends. And at the end of the day, dividends and growth drive your long-term returns.

And so investors [inaudible] strategy and it's expressed in different funds. And Tortoise has this too, and again I want to remind your listeners that a quirk of owning partnerships in a mutual fund is that if the portion of partnerships exceeds 25%, that mutual fund becomes a taxable C-corporation just like Exxon or IBM. So think of it as a taxable corporation whose business is running a portfolio if that portfolio has more than 25% of its assets in partnerships of any kind.

So that's why both Tortoise and we have funds that in some cases exceed that because investors knew that's what they were getting. And in other cases stay below the 25% to avoid that extra layer of taxation. So TYG is a taxable fund, FEN which is a First Trust fund that we took over in 2007 is a taxable because partnerships exceed 25% of the portfolio. So we have a fund as does Tortoise that are open-end funds that keep the partnerships below 25%, the ticker of ours is EMLP. I think Tortoise is TORTX, is that right, Matt?

Matthew Sallee: TORIX is the institutional fund. Jim, I appreciate the plug there, buddy.

Mike Taggart: Highly unusual, that's awesome!

James Murchie: It's very important for investors to know that. Investors are willing to give up a whole extra layer of taxation just to avoid K-1s. And today, look, the MLP structure is broken. It has no sponsorship, the valuations are terrible. We just had a spin-out of the midstream company from the old Detroit Edison, DTE Energy. And they formed it as a C-corporation. Why? Because they want to get a valuation it's better than you can get as a publicly traded partnership. The publicly traded partnerships has some really good companies in it like Enterprise and Magellan, but the whole space is tainted by the bad companies that were there.

Again, investors don't have the time to be able to tell the difference, so they buy indexes and things like that, and the index was brought down. But Matt referred to this before, there was bad corporate governance, too much money going to the general partner, too much investment, too much share issuance. And while the managements got paid well, the shareholders did not. Actually today the White House came out and said they're in support of renewable MLPs. And this was on CNBC and one of the panelists said, "Well, who cares? Because the MLP structure is so poorly valued, why would anyone want to do that? Renewable companies are trading at four times the valuation of an average MLP."

Mike Taggart: Thanks for that. Anyway, I'm going to jump in real quick because we're out of time and we got some questions here. I don't know if you're going to be able to answer them because they're to do with distributions and return of capital and distributions. But the one says, how should fund investors think about the opportunity for funds to expand their private investments? Is that a plus or a negative due to less frequent/opaque marks?

Matthew Sallee: I wouldn't view it as positive or negative in terms of the marks. It's important, what is the quality of those marks? We've been an active participant in the private investment and public equities, so basically the pipe market, you're buying shares off the market and public companies, and you're able to do that at a discount. And it's been less active recently, but over the years that's been a very consistent source of alpha. So I think that is indeed a good tool.

Jim mentioned that TYG as an example of a taxable corporation. When the valuations were much higher, we actually had a tax liability at times from trading the portfolio on those capital gains, and we've used private solar investments to manage that tax liability due to the investment that they generate. So I think private investments definitely have a place in these funds, but again I think in our view it's somewhat limited in nature. See better value in the public side right now.

James Murchie: I would say that private equity is a motor skill in and of itself. Private equity firms are staffed entirely differently. It is much more intense of terms of the research because you don't have all of these analysts crawling all over management generating the same questions and generating the same earnings models. It is just a different skillset that's extremely labor intensive. When we took over FEN in 2007, there was some private equity investments in there and I worked to get out of those things as fast as I possibly could. The people running those private equity investments were public security investors that quite frankly had no idea what they were doing, and I got out of those things as fast as we possibly could.

Mike Taggart: Interesting. Well, you know our time's up, and really when we were putting this together I really didn't think we were going to fill the hour. I apologize, I had to interject myself

more than I usually would because I think this conversation could go on for another hour and it would still be fascinating to me and I'm sure to our viewers. So I wanted to thank you all for joining us. I wanted to thank everybody in the audience for sticking around. Sorry if we didn't get to all your questions. There's John to take us out, I guess. But again, Jim, Sam, Matt, thank you very much for your time. It was great to listen to you, I learned a lot myself. Thank you again.

John Cole Scott: Again, I'll echo Mike's thanks to all of you guys. Especially with some of the craziness of today for everyone involved. You guys, thank you for the panel. Feel free if you want to turn your camera and mic off, I'll just give a quick closing remarks without the hassle of leaving and coming back.

Mike Taggart: Thanks guys.

James Murchie: Thanks for having us, Matt, good to see you. Thank you.

John Cole Scott: Until we're in person.

All right, well I was going to give the final remarks. I really want to thank you for day two of this event really focusing on the tax focus for investors and how to make it part of an income portfolio. We could never be more thankful than to our sponsors and members who our dues pay members of AICA. Without those financial resources, and guidance, and support, we would not be able to produce content like this.

Again, Michael and Michael, the moderators besides myself, excellent work for the two days of events. Everyone that was speaking and contributed on your team to promoting the event and to making more people aware, thank you as always. We do have a target in mind of October 11th for the replay of all the content. It is pending the compliance approval from the speakers, and so encourage them to hopefully push their folks along to get that to you. You should see all the video files tomorrow morning at the latest.

For those who haven't met her yet, Liz Centi has been in the room and she's a new member of the AICA team. We have a full-time membership director who's new to close-end funds but almost 20 years' experience in membership roles and non-profits. Thank her for her growth and ability to grow AICA. Wanting to remind people that we are that invite-to-speak model, nobody paid to be on stage today. We did our best to curate the best content from what's available in the market.

We do want to plug October 14th, we have the analysts and Seeking Alpha authors event. Should have the registration page up and running on Monday, and hopefully you'll be able to attend that and spread the word as well. Also want to say November 16th and 17th, a BDC event, a mix of BDCs, and analysts, and service providers for content like we did in the spring. And we're closing out for the December calendar with an interval fund again similar format to these. After lunch in the East Coast, and two to three tracks in a day so it's not as overwhelming and can work into your time and into your schedule as an advisor and investor or just in the ecosystem.

With that, John Cole Scott, the Active Investment Company Alliance. I do appreciate all of the help, all the support, and thank you as we keep growing and moving. Good day.

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https://AICalliance.org/

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