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REITS AND INFRASTRUCTURE INVESTMENT

REIT Series – Q2 Update

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TODAY'S PANEL

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CorEnergy Infrastructure Trust, Inc.

INFRASTRUCTURE INVESTMENT: A HOT TOPIC

- President Trump has called for $1.5 trillion in infrastructure spending from the public and private sectors.[1]
- Approximately 85% of the “critical” infrastructure in the United States is privately owned.[2]
- United States infrastructure is in need of updates, repairs, and replacement estimated in excess of $3.5 trillion in the near and medium term.[3]

1 Washington Post, March 29, 2018

2 U.S. Government Accountability Office Report, 2006

3 PBS NewsHour, November 17, 2016

INFRASTRUCTURE INVESTMENT

INFRASTRUCTURE INVESTMENT: A HOT TOPIC

- Major Infrastructure Investment and Repair Areas:
  - Oil & gas: $890 billion (from 2014-2025)[1]
    - Oil & gas infrastructure grew from $56 billion in 2010 to $90 billion in 2013[1]
  - Roads & Bridges: $836 billion to $2 trillion (current backlog)[2]
  - Drinking water systems: $384 billion to $1 trillion (over 25 years)[2]
  - Electricity (generation and distribution): $177 billion (through 2025)[2]
  - Rail (freight and passenger) and other transit: $90 billion (through 2020)[2]

1 IHS Global Inc., "Oil and Natural Gas Transportation and Storage Infrastructure: Status, Trends, and Economic Benefits," December 2013
2 American Society of Civil Engineers 2017 Infrastructure Report Card; CNN.com March 3, 2017.

USING THE REIT STRUCTURE WITH INFRASTRUCTURE ASSETS

WHAT INFRASTRUCTURE ASSETS CAN QUALIFY?

- A REIT can own infrastructure assets that have a passive function. For example:
  - Transmission lines, pipelines, fixed offshore drilling platforms
  - Electric Transmission/Distribution Systems
  - Storage structures (including silos and oil and gas storage tanks)
  - Renewables
    - Roof top sites, easements/leases, site pads
    - Mounts, wires and other permanent fixtures may qualify
  - Terminals
  - Salt Water Disposal Wells

USING THE REIT STRUCTURE WITH INFRASTRUCTURE ASSETS

WHAT INFRASTRUCTURE ASSETS CAN QUALIFY (CONT'D)?

- Railroad assets
- Cellular towers
  - Currently, this is the primary focus of many infrastructure REITs
- Other communications infrastructure (fiber optic cable)
- Data centers
- Ports and marinas

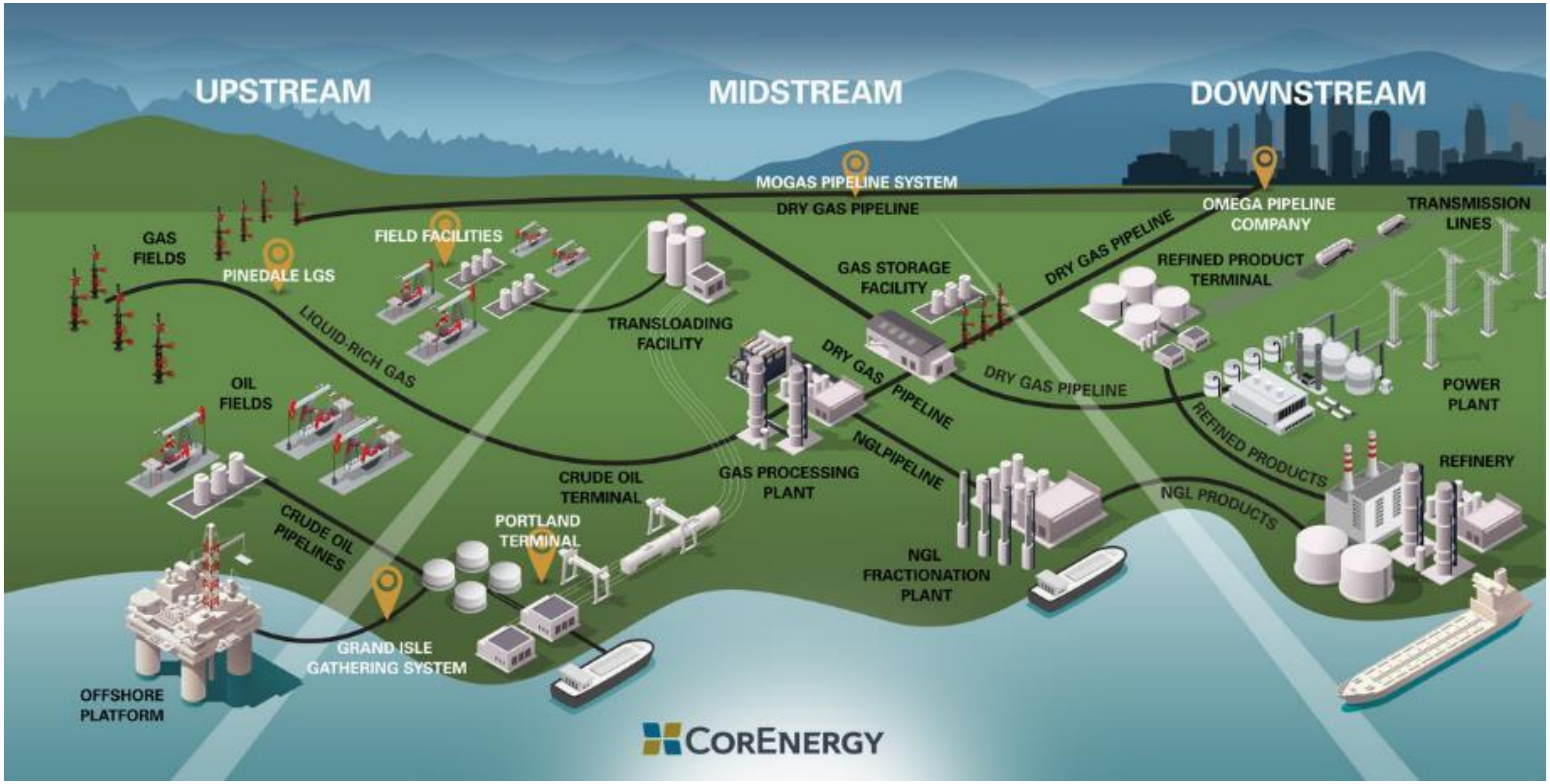
- Toll roads?
- Bridges?

USING THE REIT STRUCTURE WITH INFRASTRUCTURE ASSETS

WHAT INFRASTRUCTURE ASSETS WILL *NOT* QUALIFY?

- PV Modules in solar energy sites
- Wind turbines
- Meters and compressors in a pipeline transmission system
- Temporary drilling platforms

USING THE REIT STRUCTURE WITH INFRASTRUCTURE ASSETS



A REIT can own passive assets (or active assets through a TRS)

POTENTIAL REIT BENEFITS

WHAT ARE THE POTENTIAL BENEFITS OF REIT UTILIZATION

- Inexpensive equity financing
- Ability to monetize real estate assets
- Tax efficient for institutional investors
  - Unlike MLPs, REITs are tax-efficient for institutional investors such as tax-exempt organizations, mutual funds and non-U.S. investors
- REIT structure remains generally attractive even after assessing impact of Tax Cuts and Jobs Act (see following slides)
- REIT stockholders receive 1099s instead of K-1s
  - A REIT is not a pass-through entity
- March 2018 FERC directives will potentially adversely affect operating results for certain MLPs, most of which hold REIT-eligible assets (see following slides)
- Ability for operator to accelerate depreciation on certain assets
- Allows operator to focus capital expenditures on “non-passive assets”

REIT BASICS

REIT QUALIFYING INCOME

- Rents from qualifying real property
- Interest on mortgages on qualifying real property
- Capital gains from sales of the above

REIT BASICS

WHAT IS QUALIFYING REAL PROPERTY?

- Real Property
  - Land—includes fee, leaseholds, easements/rights of way
  - Inherently Permanent Structures (IPSs)
  - Structural Components of IPSs (but only if included with IPS)
- Passive Nature
  - Must serve a passive function and not active function
- Qualifying Non-Real Property
  - Associated Personal Property
- Use of TRS for Non-Qualifying Assets and Income
  - Investment in TRSs cannot exceed 20% of gross assets

WHAT IS RENTAL INCOME?

- Operating Lease
  - Lease must qualify as an operating lease and not a capital lease under tax rules
- Related Party Tenant Prohibition
  - Tenant cannot be materially related to REIT (no overlapping 10% or greater owners)
- Prohibition on Rents based on Net Income
  - Rent can be based on gross income

TAX CUTS AND JOBS ACT
OVERVIEW OF IMPACT ON REITS

- Treatment of Pass-Throughs (Including REITs)
  - 20% deduction on 37.0% top individual rate (resulting in 29.6% effective tax rate) with respect to qualified business income from each qualified U.S. trade or business
    - Applicable to REIT dividends (other than capital gain or qualified dividends which are already taxed at preferential rates)
    - Deduction subject to limits (importantly, limits <u>not</u> applicable to REIT dividends)
  - Pass-through rate applies to both common and preferred dividends paid by REITs
  - Pass-through rate applies to private REITs as well as public REITs

- Interest Deductibility
  - Limits net interest deduction to 30% of EBITDA through 2021, thereafter 30% of EBIT
    - Disallowed interest may be carried forward indefinitely
    - Taxpayers engaged in "real property trade or business" may elect out of limitation
  - Importantly, new rules apply to partnerships and corporations; prior section 163(j) applied only to corporations
  - Election out is <u>permanent and irrevocable</u>, so proceed with caution

TAX CUTS AND JOBS ACT
OVERVIEW OF IMPACT ON REITS

- Corporate Tax Rate
  - Reduced from 35% to 21% by TCJA
    - Reduction represents a benefit for TRSs
    - Reduction could make retention of capital gain and payment of tax a more realistic capital recycling strategy for REITs

- Technical terminations of partnerships
  - Eliminated by TCJA
    - Cuts down on tax return compliance costs but also narrows planning opportunities
    - Generally a positive for REITs because technical terminations of partnerships triggered a restart of deprecation periods on assets, resulting in reduced depreciation deductions

TAX CUTS AND JOBS ACT

DO REITS STILL MAKE SENSE IN LOWER CORPORATE RATE ENVIRONMENT?

REIT VS. C-CORP TAX EFFICIENCY

	Pre-TCJA		Post-TCJA	
	REIT	C-Corp	REIT	C-Corp
Taxable Income	100.00	100.00	100.00	100.00
Entity Level State Tax	0.00	(6.00)	0.00	(6.00)
Entity Level Federal Tax	0.00	(32.90)	(0.00)	(19.74)
Distribution to Shareholder	100.00	61.10	100.00	74.26
Shareholder State Tax	(6.00)	(3.67)	(6.00)	(4.46)
ObamaCare Tax	(3.80)	(2.32)	(3.80)	(2.82)
Shareholder Tax Federal	(37.22)	(11.49)	(29.60)	(14.85)
Net Cash to Shareholder	52.98	43.63	60.60	52.13
Total Tax	47.02	56.37	39.40	47.87
Delta vs. C-Corp	9.35		8.47	

Notes

- The above assumes a state corporate and individual tax rate of 6.0% for illustrative purposes. Increasing that rate is generally more favorable to REITs.
- Current law calculation assumes state income tax paid by individual recipient reduces federal taxable income from dividends dollar for dollar (rather than being spread among all of recipient's federal taxable income).
- Without that assumption, prior law delta vs. C-Corp. was approximately 7.71
- State and local tax deduction now capped at $10,000.
- There is a significant reduction in total tax paid and a significant increase in net cash to shareholders under TCJA vs. prior law.
- Under TCJA, advantage of REIT as compared to C-Corp. is reduced slightly as compared to current law (but is increased significantly over prior law when factoring in the elimination of deductions for state income tax (delta of 7.71 prior law vs. 8.47 under TCJA).

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TAX CUTS AND JOBS ACT
DO REITS STILL MAKE SENSE IN LOWER CORPORATE RATE ENVIRONMENT?

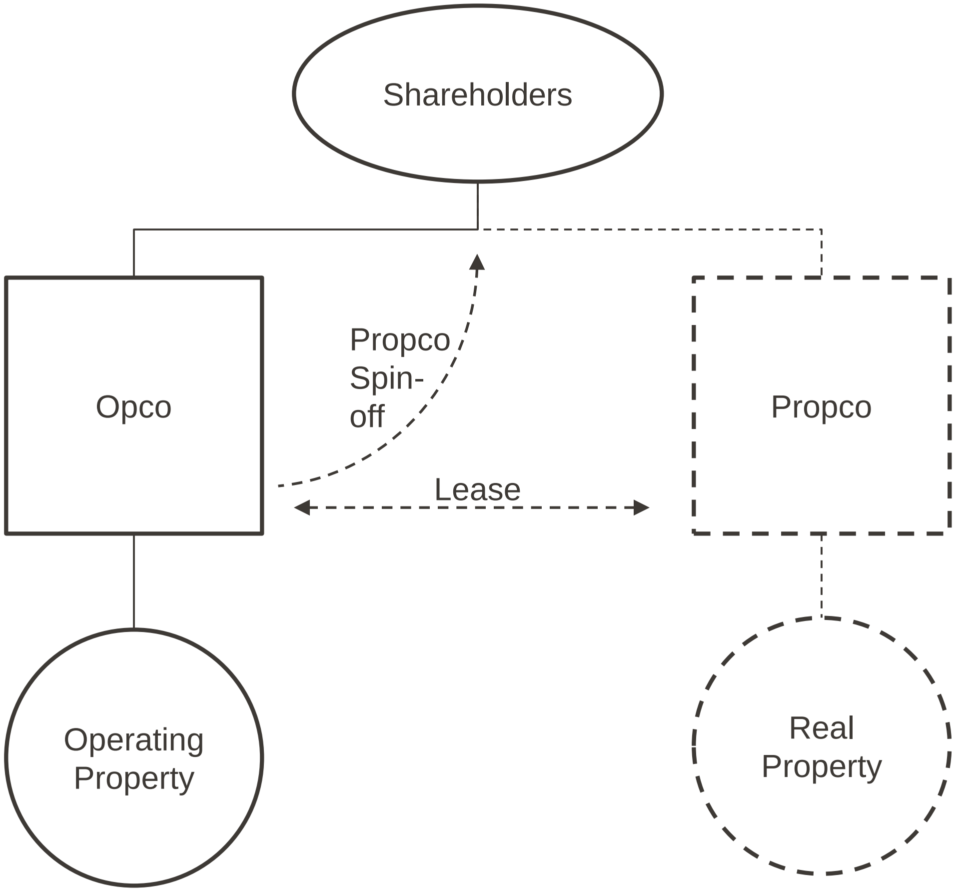
- Under all scenarios, tax-exempt investors will continue to heavily prefer REITs, as any corporate tax paid (even at a reduced rate) reduces their returns
  - TCJA disallows aggregation (netting of gains and losses) of UBTI from different sources, making REITs' function as an efficient UBTI blocker even more important
- Foreign investors will similarly continue to prefer REITs for investing in real estate as any corporate-level tax paid reduces their return and C-Corporations are not treated any more favorably than REITs with respect to outbound withholding on dividends
  - Foreign investors may still exit projects tax-free through the sale of domestically-controlled REIT shares
- Electing corporate status is a one way street; re-electing REIT status down the road comes with significant difficulties
  - E&P Purge
  - Sting tax on assets
  - Lockout period on re-electing REIT status
- How "permanent" is the 21% corporate rate?
  - Changing landscape related to tax reform and subsequent Congresses and Presidents-risk of buyers remorse
  - TCJA passed with no Dem votes; politically easier to raise corporate rate in the future

INFRASTRUCTURE REITS: POTENTIAL STRUCTURES

WHAT STRUCTURES CAN BE FACILITATED WITH A REIT?

- Propco/Opco Spin-Off
  - PATH Act prohibition on tax-free REIT spin-offs
- Sale-Leaseback
- Drop-Down/Contribution
- Mortgages
  - Third Party Loans
  - Loans to TRSs
- C-Corp conversions
  - Impact of Temporary Regulations on C-Corp conversions

INFRASTRUCTURE REITS: POTENTIAL STRUCTURES
SPIN-OFF



- Corporation engaged in real estate intensive business ("Opco") contributes real property assets to new subsidiary ("Propco")
- Opco distributes stock of Propco to public in a taxable spinoff (with limited exceptions)
- Propco elects REIT status
- Could also be structured as Propco spin-off of Opco
- REIT spin-offs of C-Corp and vice versa denied tax-free treatment under PATH Act

INFRASTRUCTURE REITS: POTENTIAL STRUCTURES
SPIN-OFF

EXAMPLES:

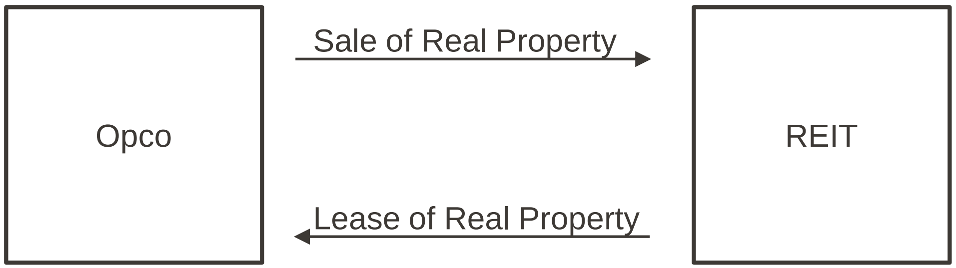
Windstream Holdings (UNITI Group Inc.)

- Windstream spun off the predecessor entity to Uniti Group in a tax-free transaction, with Uniti owning its communication distribution systems.
- Distribution systems were triple-net leased back to Windstream Holdings.

Darden Restaurants (Four Corners Property Trust)

- Darden spun-off Four Corners in a tax-free transaction, with Four Corners owning its restaurant properties.
- Four Corners triple-net leased the properties back to Darden to operate.

INFRASTRUCTURE REITS: POTENTIAL STRUCTURES
SALE-LEASEBACK



- Corporation engaged in real estate-intensive business sells real property assets to REIT
- Opco leases the real property back from the REIT

EXAMPLES:

CorEnergy Infrastructure Trust, Inc.

- Conducts sale-leasebacks with energy companies and generally triple-net leases the assets back to the seller.

Pinedale LGS

Acquired from / leased to Ultra Petroleum Corp in December 2012

Grand Isle Gathering System

Acquired from / leased to Energy XXI Gulf Coast in June 2015

Portland Terminal

Property identified by / leased to Arc Logistics (now Zenith Energy) in January 2014

- **National Retail Properties**
- Conducts sale-leasebacks with convenience store operators and generally triple-net leases the assets back to the seller.

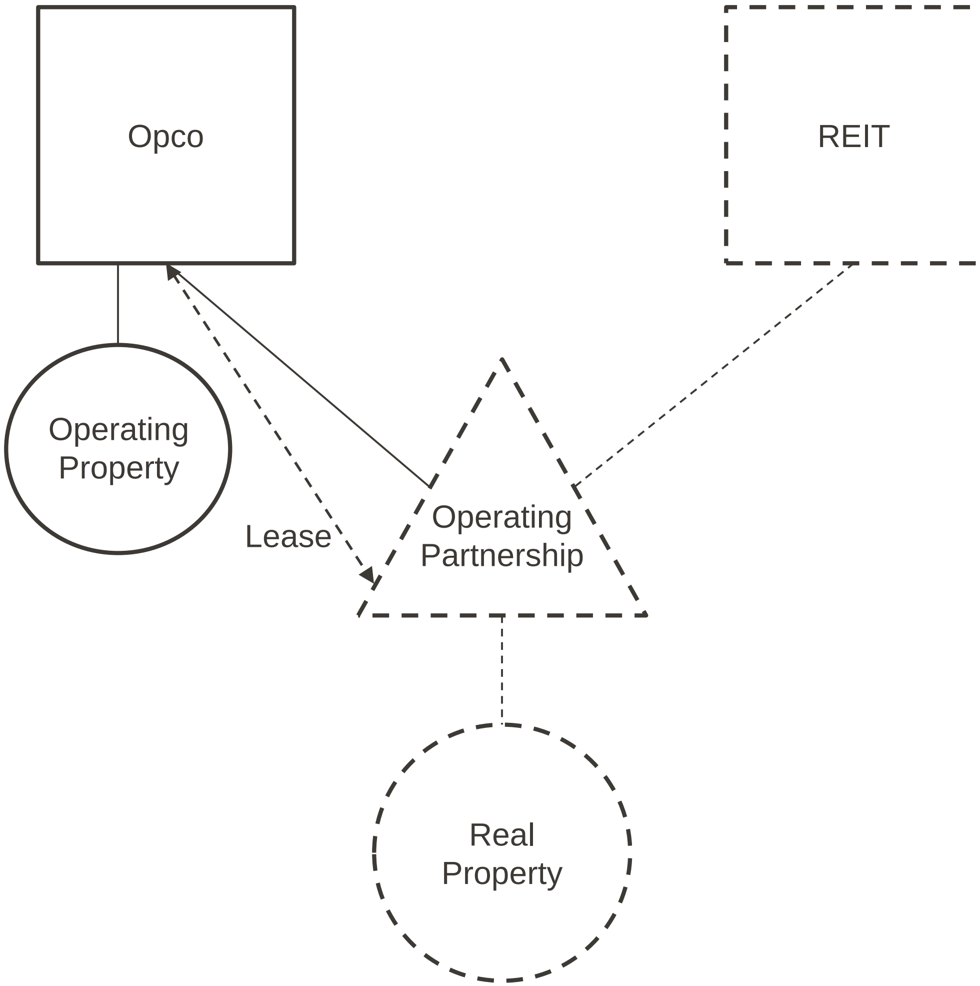
Illustrative Oil Pipeline Lease Structure (REIT leasing to Operator)

- **Leased Property**: Pipeline assets (system of pipelines, storage tanks, collection and separation facilities, salt water disposal wells and facilities, and related properties, facilities, equipment and rights) and related interconnection agreements.
- **Typical Term**: 10-15 years, one renewal option for 5-10 years or 75% of estimated remaining useful life of the pipeline assets.
- **Typical Rent Structure**: Rent paid has a "Minimum Rent" component and a "Variable Rent" component; together, they comprise the Base Rent payable monthly.
  - **Minimum Rent**: a monthly amount varying between $X million and $Y million (depending on operating costs, Brent Futures prices, reserve life, agreed volumes and other assumptions as of the lease date for each month during the term).
  - **Variable rent**: the lesser of (a) 10% of Excess Oil Revenue for such month (or portion thereof) and (b) 28% of Base Rent (i.e., 38.9% of Minimum Rent) for such month (or portion thereof).
  - **Excess Oil Revenue** means the greater of (a) zero or (b) Actual Oil Revenue for such month (or portion thereof) minus Base Oil Revenue for such month (or portion thereof). Base Oil Revenue varies based upon agreed volumes and Brent Futures prices as of the lease date or another agreed date.
- **Other terms**: Tenant has a ROFR on Landlord's proposed sale of the leased property; there are also certain other limitations on assignment and transfer by each party.

Parallel non-infrastructure example: Sale-leaseback or build-to-suit with forward commitment to purchase large distribution facilities

INFRASTRUCTURE REITS: POTENTIAL STRUCTURES

DROP DOWN/CONTRIBUTION



- Opco forms a joint venture with an existing or newly formed REIT
- REIT raises funds from equity offering and contributes cash to operating partnership for interests therein
- Opco contributes real property to the operating partnership joint venture in exchange for interests therein and, potentially, cash
- Operating partnership leases properties to sub of Opco. No partner to partner attribution under related-party rent rules.

DROP DOWN/CONTRIBUTIONS

EXAMPLES:

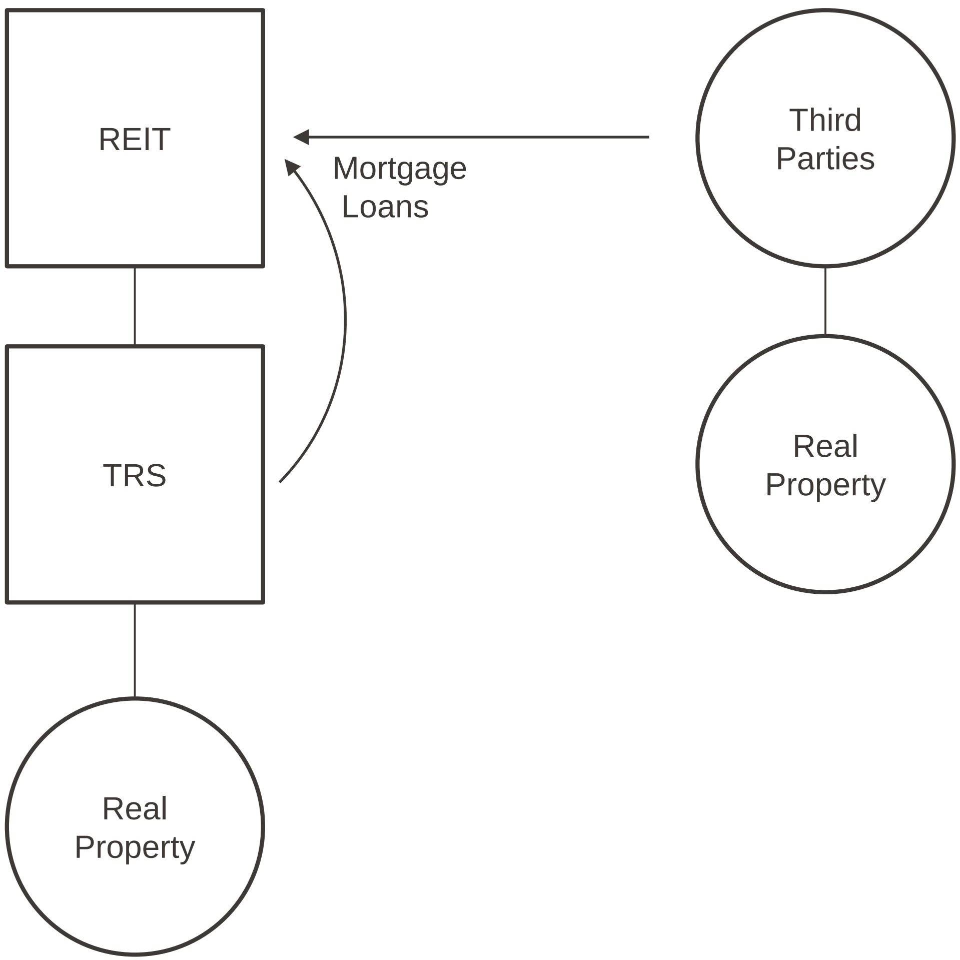
MGM Resorts/MGM Growth Properties

- MGM Resorts contributes property (and associated debt) to operating partnership of newly-formed REIT (MGM Growth Properties) in exchange for OP Units.
- Operating partnership leases casino properties back to subsidiaries of MGM Resorts.
- MGM Growth Properties conducts IPO; pays down assumed debt with combination of IPO proceeds and refinancing.

Hudson Bay/Simon Properties

- Hudson Bay contributes department store properties to newly-formed JV with Simon Properties.
- Simon Properties contributes cash to JV.
- Hudson Bay takes cash distribution from JV.
- JV leases department store properties back to Hudson Bay.

INFRASTRUCTURE REITS: POTENTIAL STRUCTURES
MORTGAGES



- REIT holds real-estate mortgage loans from third parties or, to limited extent, from TRS sub
- This strategy may be executed in conjunction with the other strategies mentioned in this presentation.

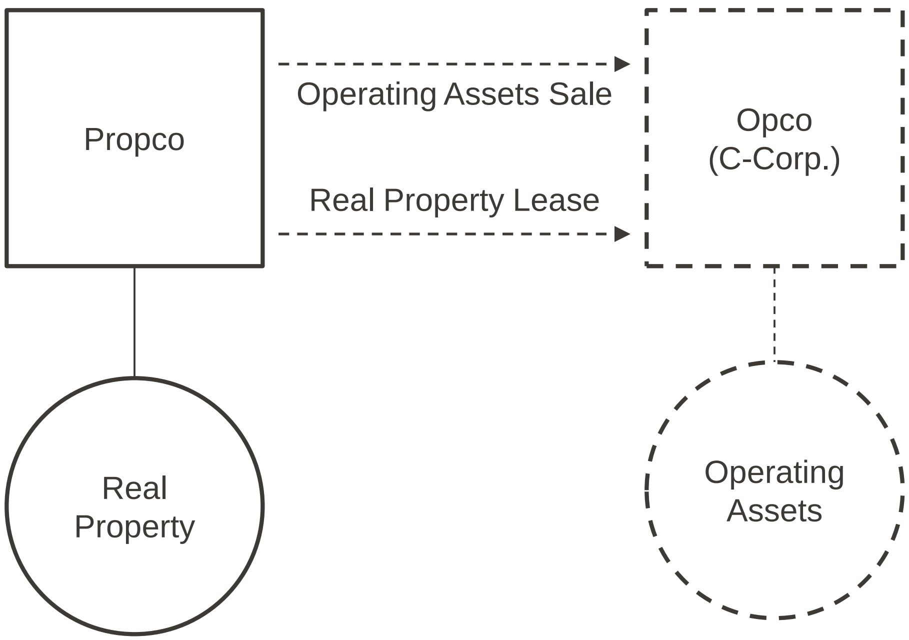
INFRASTRUCTURE REITS: POTENTIAL STRUCTURES
MORTGAGES

EXAMPLES:

Hannon Armstrong Sustainable Infrastructure Capital Inc.

- Lends on renewable energy and energy efficiency projects.
- Lending on real estate assets done directly by REIT.
- Lending on non-real estate assets done through TRS.

INFRASTRUCTURE REITS: POTENTIAL STRUCTURES
C-CORP. CONVERSION



- Corporation with real property intensive business ("Propco") sells operating assets to unrelated party ("Opco") and Propco leases real property to Opco, who operates the business
- Propco makes a REIT election
- Temporary Regulations issued in June 2016 require immediate taxation on built-in gain if C-Corp. was spun-off in tax-free spin in prior 5 years.
- Otherwise, "Sting Tax" period runs for 5 years.

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INFRASTRUCTURE REITS: POTENTIAL STRUCTURES
C-CORP. CONVERSION

EXAMPLES:

American Tower Corporation

- REIT conversion as of 1/1/12
- Leases space to wireless providers
- Utilized TRSs to continue to operate non-REIT compliance businesses
- E&P Study to ensure C-Corp. E&P had been distributed.

POTENTIAL REIT BENEFITS
OVERVIEW OF MARCH 2018 FERC NOTICE OF PROPOSED RULEMAKING

- March 15, 2018—FERC issued a suite of directives
  - Primary headline: FERC will disallow MLPs from recovering an income tax allowance in cost-of-service rates
    - Will potentially adversely affect MLPs that were previously able to use the income tax allowance in computing cost-of-service rates
    - Limits:
      - Applicable only in certain circumstances (see next slide) and only applicable to FERC-regulated assets (generally, liquids pipelines, gas pipelines and electric utilities)
      - Reduction of 2018 corporate tax rate from 35% to 21% by the Tax Cuts and Jobs Act reduces net impact

POTENTIAL REIT BENEFITS

OVERVIEW OF MARCH 2018 FERC NOTICE OF PROPOSED RULEMAKING

- Impact on MLPs of FERC directives depends on rate type
  - Cost-of-service rates—associated revenues will likely decrease
  - Settlement rates subject to a rate moratorium—no changes expected to these rates until expiration of rate moratorium
  - No current changes expected to:
    - Market-based rates
    - Negotiated rates
    - Discount rates (that remain below the cost-of-service rate and not tied to cost-of-service rates)
  - Index rates to next be adjusted by FERC effective in 2021

POTENTIAL REIT BENEFITS
OVERVIEW OF MARCH 2018 FERC NOTICE OF PROPOSED RULEMAKING

- Potential Impact on REITs of FERC directives
  - Certain assets held by affected MLPs are eligible to be held by REITs, although REITs must generally lease such assets to operators
  - In addition, a Taxable REIT Subsidiary (TRS) can operate FERC-regulated assets within the TRS size limits under the REIT rules
  - Though the allocation of general REIT expenses to a TRS is limited, there may be cost-efficient structures available

INFRASTRUCTURE REITS
WHO ARE SOME OF THE PLAYERS?

CorEnergy Infrastructure Trust, Inc. (NYSE: CORR)

- Market Cap: Approx. $443 million
- Dividend & Yield: $3.00 per sh / Approx. 8.22%
- Assets: Midstream and downstream (pipelines, storage terminals, rail terminals and gas and electric transmission and distribution assets) and loans secured by energy infrastructure.

InfraREIT, Inc. (NYSE: HIFR)

- Market Cap: Approx. $1.222 billion
- Dividend & Yield: $1.00 per sh / Approx. 5.04%
- Assets: Electricity delivery infrastructure assets in Texas and southwestern U.S.

WHO ARE SOME OF THE PLAYERS?

Hannon Armstrong Sustainable Infrastructure Capital, Inc. (NYSE: HASI)

- Market Cap: Approx. $1.01 billion
- Dividend & Yield: $1.32 per sh / Approx. 6.84%
- Assets: Loans secured by energy infrastructure and renewable assets.

INFRASTRUCTURE REITS
WHO ARE SOME OF THE PLAYERS?

Uniti Group, Inc. (Nasdaq: UNIT)

- Successor to spin-off from Windstream Holdings, Inc.
- Market Cap: Approx. $2.958 billion
- Dividend & Yield: $2.40 per sh / Approx 14.74%
- Assets: Fiber optic broadband networks, wireless communications towers, copper and coaxial broadband networks and data centers.

THANK YOU

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