Energy Programs and Your Portfolio

A traditional investment portfolio contains a combination of stocks, bonds, cash or cash equivalents, and the mutual funds or exchange traded funds (ETFs) that invest in those asset classes.

While some mix of traditional asset classes is likely to yield satisfactory investment returns for the average investor, you may also look for non-traditional opportunities, commonly known as alternative investments, to create a more comprehensive portfolio and address your specific investment needs. For example, you might consider an investment in various programs focused on energy to diversify your investment portfolio and potential sources of income.

You'll want to be sure you understand the risks as well as the potential advantages of investing in energy programs. You should research the up-front fees that apply and the possibility of additional fees during the holding period. Then, with your financial advisor, you can investigate whether an energy program can help you achieve your objectives.

Types of Energy Programs

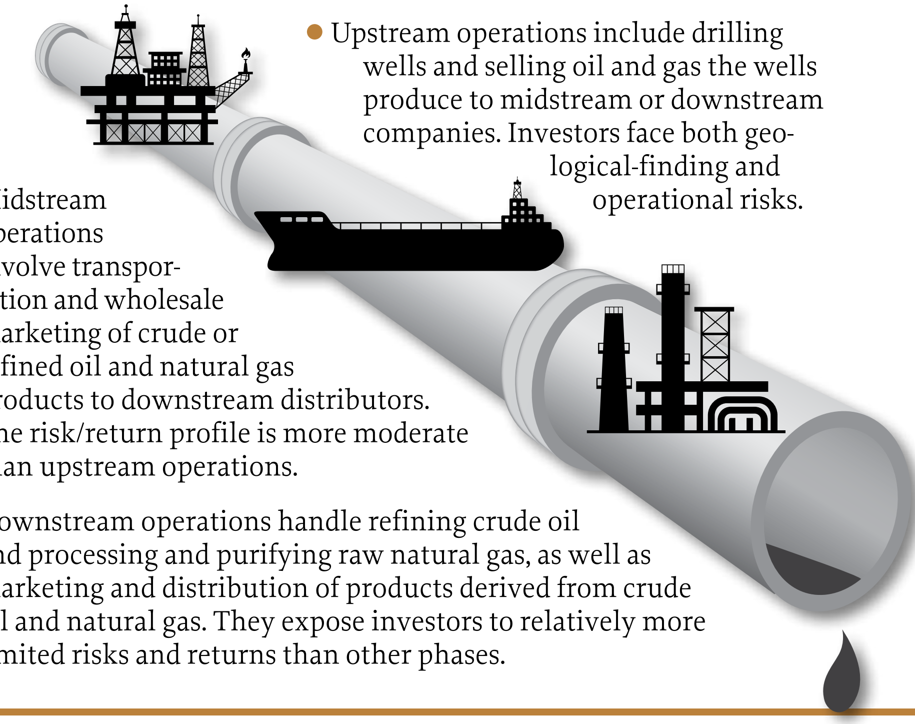
Partnership programs provide investors the opportunity to share in the net revenues of the partnership. These revenues may be distributed to investors through periodic cash payments and, in some programs, through an attempt to liquidate the portfolio at a future date.

In addition, partnership programs may have certain tax advantages. Investors may qualify for income tax benefits that derive from deductions for intangible drilling costs (IDCs), tangible equipment costs, and depletion. It should be noted, however, that while general partners may use drilling-related deductions to offset both active and passive income, limited partners may use deductions to offset passive income only. You should always discuss any tax consequences of this investment with a qualified tax professional.

Another way to make an investment in energy is through a Business Development Company. An energy-focused BDC is a closed-end investment company that invests in private or thinly traded. US companies with limited access to capital that are engaged in upstream, midstream, or downstream energy operations. BDCs can be either traded or non-traded. If BDCs may be of interest, please ask your advisor for a copy of Guide to Understanding BDCs where you can learn more about this type of investment.

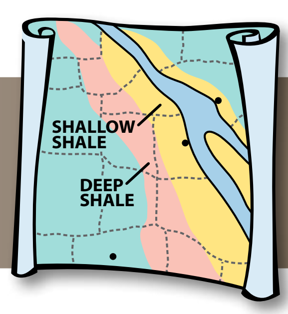
The Energy Industry

Energy programs provide the opportunity to invest in different operation phases, or segments, of the oil and gas industry, from exploration and production to processing and distribution.



- Upstream operations include drilling wells and selling oil and gas the wells produce to midstream or downstream companies. Investors face both geological-finding and operational risks.
- Midstream operations involve transportation and wholesale marketing of crude or refined oil and natural gas products to downstream distributors. The risk/return profile is more moderate than upstream operations.
- Downstream operations handle refining crude oil and processing and purifying raw natural gas, as well as marketing and distribution of products derived from crude oil and natural gas. They expose investors to relatively more limited risks and returns than other phases.

The Lifecycle of Energy Projects

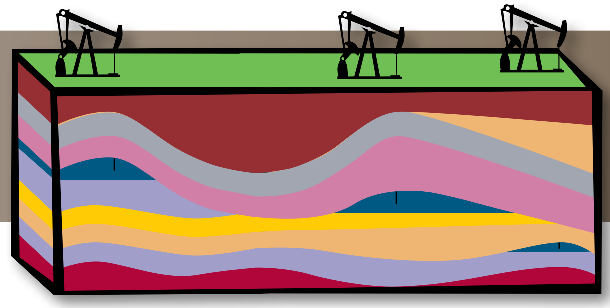


Stage 1: Conception

Before drilling can begin, a project must be conceived and evaluated. This includes reviewing various types of geological, technical, and engineering-related data to determine whether or not a particular area has the potential to produce economic quantities of oil and gas.

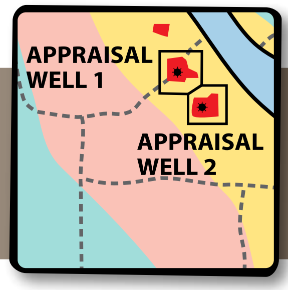
Stage 2: Leasing

If its investigation indicates, from technical and legal perspectives, that drilling wells within the area of interest can potentially produce an economic return, the company directs its land personnel to undertake efforts to lease the acreage needed to drill test wells or exploration wells.



Stage 3: Evaluation

Estimates of future production rates in an area will be undertaken by reservoir engineers using methodology customary in the oil and gas industry. One of those methods might include a field appraisal undertaken to establish the size of the field and the most appropriate production methods. Appraisal wells are drilled to confirm the size and structure of the field.



Stage 4: Development

When the project is judged technically and commercially viable, a development plan is submitted to the relevant authorities for approval. In this phase, developmental wells are drilled on or close to areas that have proven productive, and where the new leases are believed to encompass the same geologic feature.

Stage 5: Production

As raw hydrocarbons are produced from the wells, the oil or gas is routed to nearby production facilities for processing and export. Once the project is on-line, operations are gradually increased until a field reaches peak production. This is maintained for a number of years before production starts to decline.

Advocating Direct Investments Through Education

IPA
Investment Program Association

A Word About Risk

Investing in energy programs poses unique risks. Unlike real estate or business equipment and facilities, which investors can see before making a commitment, the qualities of the oil and gas actually located within an area of interest cannot be known with certainty until the drilling process is completed, the wells are placed on-line, and are actually producing quantities of oil and natural gas.

In cases where the initial operations are successful, it is possible that unforeseen mechanical, environmental, and transportation problems will arise that compromise the economic return potential of the project. Additionally, oil and natural gas reserve estimates and cash flow projections can and often do vary considerably from what is realized over a long-term investment period.

The purported income tax benefits associated with drilling programs require investors to accept the liability exposure of a general partner to realize active income sources. Investors with otherwise higher investment risk tolerances may not want to accept the risk of exposing their other portfolio assets to losses if the partnership program were to encounter operational liabilities. While there are a number of measures to help mitigate these risks, willingness to accept liability risk should be given significant consideration.

For oil and gas programs designed to invest in working interests or royalties in producing wells, the potential exists for investment losses from a number of factors that include oil and natural gas pricing movements, reserve reporting inaccuracies, and the general effects of depletion. Thus, while an income-designed oil and gas program may be structured to provide investors with opportunities for ongoing cash flows over a long-term investment period, these programs are also subject to investment risks that can potentially compromise the opportunities for a return on investment and the ability to realize a return of invested capital.

Is an Energy Program Right for You?

The oil and natural gas business is a multifaceted global industry that impacts all aspects of life. Oil and natural gas provide the world's 6.9 billion people with 60% of their daily energy needs.

Energy programs provide investors with the opportunity to engage this wide ranging and impactful industry. From the harvesting of energy sources to the delivery of energy to consumers, these programs can be a diversifying asset to qualified clients.

If investing in energy seems attractive to you, talk to your financial advisor about how energy programs may fit into your investment portfolio. However, oil and gas drilling programs are not generally suitable for investors with either low investment-risk tolerance or who cannot accept the idea that they may incur a significant loss of their invested capital. Additionally, as oil and gas programs have indefinite investment holding periods, these investments also may not be suitable for retail investors with special liquidity needs.

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Guide to Understanding Energy Programs

An investment in knowledge pays the best interest.
— Benjamin Franklin