Questions and Answers regarding the Managed Distribution Plan

Question 1: What is a Managed Distribution Plan?

Answer: A Managed Distribution Plan is one in which common shareholders receive a consistent, but not guaranteed, periodic cash payment, regardless of when or whether income is earned or capital gains are realized. Such a policy recognizes that many investors are willing to accept the higher price volatility of equity investments, but desire a stable level of cash distributions available to them each month for reinvestment or other purposes. The Plan adopted by your Fund’s Board of Directors provides for a continuation of monthly distributions of 6.5 cents per share, which amounts to 78 cents annually, subject to the Board’s right to suspend, modify, or terminate the Plan without notice at any time.

Question 2: Why is the Fund implementing a Managed Distribution Plan at this time?

Answer: For the past several years, less current income has been earned on the Fund’s traditional investment holdings because interest rates have been at historically low levels, utility common stock dividend yields have been well below their long-term average, and income earned on the Fund’s leverage, while still beneficial, has dropped. Consequently, there has been a smaller amount of current income available to distribute to shareholders. Initially, in order to sustain the monthly distribution level, the Fund used strategies designed to capture dividend income. However, beginning in 2004, Fund management curtailed the use of dividend capture strategies and made increased use of realized capital gains. Because these capital gains were fully offset by the Fund’s tax loss carryforwards, they have been characterized as ordinary income, rather than as capital gains, under the Internal Revenue Code. Once the Fund utilizes all of its tax loss carryforwards, the timing of which is impossible to predict, and in the absence of an increase in the yields earned on Fund investments, the Fund’s monthly distributions to shareholders may include short- and long-term capital gains and/or a portion of non-taxable return of capital in order to maintain the distribution rate.

The Investment Company Act of 1940 (the “1940 Act”) generally prohibits investment companies from distributing long-term capital gains (as defined by the Internal Revenue Code) more often than once every twelve months. However, funds that have adopted a Managed Distribution Plan often seek exemptive relief from the Securities and Exchange Commission (“SEC”), permitting them to distribute long-term capital gains more than once a year. In order to potentially augment the sources from which your Fund’s monthly distribution can be paid, the Fund’s Board of Directors, at the same time that it adopted a Managed Distribution Plan, also authorized the Fund to apply to the SEC for such exemptive relief.

Question 3: What approvals does the Fund need from the SEC in order to implement the Managed Distribution Plan?

Answer: Investment company distributions are governed by Section 19(b) of the 1940 Act and Rule 19b-1 under the 1940 Act. Under Section 19(b), investment companies are limited to one distribution per year of long-term capital gains (as defined in the Internal Revenue Code), subject to certain exceptions contained in Rule 19b-1. Because the Fund currently offsets its long-term capital gains with tax loss carryforwards, distributions made pursuant to the Managed Distribution Plan do not consist of long-term capital gains (as defined in the Internal Revenue Code). For this reason, exemptive relief from the SEC is not needed in the near term. However, if and when the Fund exhausts its tax loss carryforwards, it will likely need to utilize net realized long-term capital gains to maintain a steady distribution, and will therefore require exemptive relief from Section 19(b)
and Rule 19b-1 in order to distribute long-term capital gains more than once in a 12-month period. Having a Board-approved Managed Distribution Plan in place is generally a prerequisite for the SEC to consider exemptive relief from Section 19(b) of the 1940 Act.

**Question 4: How does the SEC handle requests for exemptive relief from Section 19(b) of the 1940 Act?**

**Answer:** Historically, investment companies that wished to implement a managed distribution plan allowing for multiple capital gain distributions in a 12-month period have sought exemptive relief from Section 19(b) and Rule 19b-1. In October 2006, the SEC staff announced a new set of conditions to be included in applications for exemptive orders. The SEC staff has stated that the new conditions are intended to ensure that funds will provide fund investors and others with enhanced disclosure about the sources of distributions made under a Managed Distribution Plan and about the fund's total return relative to the distribution rate under the Plan. Your Fund plans to file an application with the SEC, in accordance with the conditions set forth by the SEC staff, so that the Fund will be able to maintain the Managed Distribution Plan even after the Fund's capital loss carryforwards are exhausted. The SEC staff’s conditions (which were further amended in December 2006) are detailed in the answer to Question 5 below.

**Question 5: What information does the SEC require the Board to consider as part of the application process for exemptive relief from Section 19(b) of the 1940 Act?**

**Answer:** First, the Board is required to consider: (1) the details of the proposed Managed Distribution Plan (including the amount of the periodic, level distribution), the purpose of the Plan, and the right of the Board to amend or terminate the Plan at any time without prior notice to Fund shareholders; (2) how adoption and implementation of the Plan are consistent with the Fund’s investment objectives and policies and are in the best interests of the Fund and its shareholders; (3) any potential or actual conflict of interest that the Adviser or any affiliated persons of the Fund or Adviser may have relating to the adoption or implementation of the Plan; (4) any foreseeable material effect of the Plan on the Fund’s long-term total return in relation to market price and net asset value (“NAV”); and (5) whether the rate of distribution under the Plan will exceed the Fund’s total expected return in relation to NAV.

Second, from a compliance standpoint, the Board is required to consider the policies and procedures that the Fund’s Administrator and Adviser propose to adopt relating to the Plan. Specifically, the compliance procedures relating to the Plan must: (1) be designed to provide reasonable assurance that all notices required to be sent to Fund shareholders pursuant to Section 19 of the 1940 Act include all the required disclosures; (2) require that the Fund keep records that demonstrate its compliance with all of the conditions of Section 19 of the 1940 Act; (3) provide for the Fund’s Chief Compliance Officer to review the adequacy of the policies and procedures proposed by the Fund’s Administrator and Adviser, determine whether the Fund and the Fund’s Adviser have complied with the conditions set out by the SEC in the exemptive order, and report the results of the review to the Board of Directors at least once every three months or at the next regularly scheduled quarterly board meeting; (4) address the course of action for widespread public disclosure of information regarding the Fund’s periodic distributions via press releases, SEC filings, website postings, and inclusion in Fund information, communications, and reports to shareholders, beneficial owners, and potential shareholders; (5) address monitoring the trading in the Fund's common stock so that the Board of Directors may readdress the appropriateness of the Plan and its benefits to Fund shareholders if the Fund’s common stock has traded at greater than a 10% premium to NAV and/or the Fund's annualized distribution rate, expressed as a percentage of NAV, is greater than the Fund's average annual total return in relation to the change in NAV over a prescribed period of time.
Question 6: What are the primary advantages of a Managed Distribution Plan?

Answer: A managed distribution plan allows a fund to provide to its common shareholders a regular, periodic distribution that is not dependent on the timing or amount of income earned or capital gains realized by the fund. This type of distribution plan recognizes that many investors are willing to accept the higher price volatility of equity investments but also like to receive a consistent level of cash distributions each month for reinvestment or other purposes. It also reduces share price volatility associated with a potentially large one-time distribution. Further, Lipper Analytical Services (“Lipper”) data indicate that managed distribution policies tend to have a positive effect on supporting a closed-end fund’s market price in relation to its NAV. Even though your Fund historically has traded at a premium, there can be no assurance that the premium will persist over the long term.

To the extent that the Fund distributes long-term capital gains, either annually or, if the Fund is granted exemptive relief from Section 19(b) of the 1940 Act, the tax effects will be favorable under current tax law, as the applicable tax rate will be the lower capital gains tax rate instead of the rate applied to ordinary income.

Question 7: What are the primary disadvantages of a Managed Distribution Plan?

Answer: One disadvantage of the Managed Distribution Plan is a negative tax impact on shareholders when the Fund’s distribution includes capital loss carryforwards offset by realized capital gains. (See Question 11 below.) Distributions of offset capital gains are characterized under the Internal Revenue Code as ordinary income to shareholders, and are taxed as such, rather than at the more favorable rate on long-term capital gains. In addition, the Managed Distribution Plan may affect the Fund’s portfolio management strategy, which is discussed in Question 8 below. If the Fund’s total return is less than the annual distribution, the Managed Distribution Plan could shrink the assets of the Fund over time and thus increase the Fund’s expense ratio (i.e., the Fund’s fixed expenses will be spread over a smaller pool of assets). Another potential disadvantage of the Managed Distribution Plan is that it is subject to modification, suspension or termination at any time, without notice, by the Board. This is discussed in more detail in Question 9 below. Finally, a managed distribution that contains a return of capital will require shareholders to adjust their cost basis by the amount of each return of capital so that when they sell their shares, their cost basis will be lower. This will add to the recordkeeping requirements of shareholders.

Advantages and disadvantages notwithstanding, the Fund has no control over the capital gains it may be forced to realize because of unexpected tender offers or mergers of the issuers of its underlying stockholdings. In addition, the components of dividends received from real estate investment trusts (REITs) – ordinary income, capital gains, and return of capital – cannot be determined by the Fund at the time of distribution. Indeed, the REITs themselves do not know the exact percentage breakdown of those components until after the end of the calendar year, at which time REIT security holders (including the Fund) are notified. The tax characteristics of the REIT dividend portion of the Fund’s total distribution for a year are then made available to Fund shareholders, but are not within the control of the Fund.

Question 8: Will the Managed Distribution Plan impact the way in which the Fund is managed?

Answer: Adoption of the Plan is not expected to materially change the portfolio management strategy of the Fund. The Fund’s primary investment objectives continue to be current income and growth in income; capital appreciation remains a secondary objective. The Fund seeks to achieve these objectives by investing in a diversified portfolio of equity and fixed income securities of companies in the public utilities industry. Under normal conditions, the Fund’s investment policies require the Fund to invest at least 65% of its assets in companies engaged in the production, transmission, or distribution of electric energy, gas, or telephone services. The Adviser does
not expect to change the makeup of the portfolio because of the adoption of a managed distribution policy; rather, the Fund will maintain its traditional focus on the securities of high-quality, income-generating utility companies. The Adviser may manage the portfolio slightly differently than in the absence of the Managed Distribution Plan, but not in such a way that is likely to negatively impact shareholders. For instance, the Adviser may realize a loss in a security by selling it in order to offset realized capital gains; absent the Managed Distribution Plan, the Advisers might not have caused the Fund to realize the loss. This would result in slightly higher portfolio turnover with a small cost of trading. However, the Adviser will not retain positions that it believes should be sold based on fundamental analysis of the underlying company.

**Question 9: Under what circumstances can the Managed Distribution Plan be terminated or suspended?**

**Answer:** The Managed Distribution Plan can be modified, suspended, or terminated at any time by the Board, without any notice to or approval by shareholders. Because the Managed Distribution Plan has been implemented prior to receiving exemptive relief from Section 19(b) and Rule 19b-1 of the 1940 Act, its continuation without violating Section 19(b) and Rule 19b-1 will be dependent on a number of factors over which the Fund has no control. For this reason, the Fund has the flexibility to modify, suspend, or terminate the Managed Distribution Plan immediately if the Board deems such action to be in the best interests of the Fund and its shareholders. For instance, the Board may modify, suspend, or terminate the Managed Distribution Plan if the Plan has the effect of shrinking the Fund’s assets to a level that is determined to be detrimental to Fund shareholders. The suspension or termination of the Managed Distribution Plan could have the effect of creating a trading discount (if the Fund is trading at or above NAV) or widening an existing trading discount.

**Question 10: Are the managed distribution payments considered “yield”?**

**Answer:** Not necessarily. You should not draw any conclusions about the Fund’s investment performance based on the magnitude of the distribution. Yield is a measure of net investment income, relative to the share price, that is distributed to the Fund’s shareholders. A distribution of capital gains, for example, is not considered net investment income. Neither is a return of capital. Therefore, managed distributions consisting of capital gains and/or return of capital do not result in a higher yield or a high yield fund.

**Question 11: Will the Managed Distribution Plan result in any additional administrative consequences or have tax effects for shareholders?**

**Answer:** There would be an added recordkeeping obligation for shareholders if at some point the distributions contain a return of capital component. Return of capital is not taxable to shareholders in the year it is paid. Rather, shareholders are required to reduce the cost basis of their shares by the amount of the return of capital so that, when the shares are ultimately sold, they will have properly accounted for the return of capital. Such an adjustment may cause a shareholder’s gain to be greater, or loss to be smaller, depending on the sales proceeds received. For example, assume a shareholder bought shares in the Fund for $10.00 per share and then received dividends from the Fund that included $1.00 per share of return of capital. At that point, the cost basis should be adjusted down to $9.00 per share. If the shareholder subsequently sells the shares for $10.50 each, the gain is $1.50 per share, taxed at the long-term capital gains tax rate. Essentially, a return of capital defers shareholders’ tax liability until the shares are sold. Shareholders who hold their shares in non-taxable accounts such as IRAs will not need to make any adjustments in the cost basis.
Other tax effects of the Plan are minimal. As described in the answers to Questions 2, 3, and 7 above, if the Fund has net realized long-term capital gains and a tax loss carryforward position, as has been the case over the past few years, distributions of those gains are treated as ordinary income to shareholders and taxed at the ordinary income tax rate under the Internal Revenue Code. However, a long-term capital gains distribution, regardless of whether it is disbursed monthly or once annually, will be taxed at the long-term capital gain tax rate under the Internal Revenue Code.

The foregoing is not intended to be a complete discussion of the tax consequences of the Managed Distribution Plan and shareholders are urged to seek their own professional tax advice regarding this matter. The Fund will send you a Form 1099-DIV following the end of each calendar year that will tell you how to report Fund distributions for federal income tax purposes.

**Question 12: Why do shareholders receive a 19(a) Notice?**

Section 19(a) of the 1940 Act provides that if a registered investment company’s distributions are composed of a source other than net income earned on the underlying holdings, the distribution must be accompanied by a written statement (a “19(a) Notice”) that adequately discloses the sources of the distribution. Net realized short- and long-term capital gains and return of capital are examples of other sources from which the Fund’s distribution may be paid. Therefore, in accordance with the 1940 Act, the Fund provides a 19(a) Notice to shareholders, detailing the proportion of the distribution represented by net investment income, net realized short- and/or long-term capital gains, and return of capital, as pertinent to the period covered by the distribution.

Because the 19(a) Notice would alert shareholders if at some point distributions contain a return of capital, it would also alert shareholders that they might have a record keeping obligation (as discussed in Question 11). It is important for shareholders to understand that the calculations in the 19(a) Notice are based on Generally Accepted Accounting Principles (GAAP); on the other hand, the tax characteristics of distributions detailed on the 1099-DIV form that shareholders receive after the end of a calendar year are based on the Internal Revenue Code, which may or may not be equivalent to the GAAP treatment. Shareholders are urged to seek their own professional tax advice regarding this distinction.

The 19(a) Notice also assists you in understanding the Fund’s yield and return characteristics. You should not draw any conclusions about the Fund’s investment performance simply based on the magnitude of the distribution. Yield is a measure of net investment income, relative to the share price, that is distributed to the Fund’s shareholders. A distribution of capital gains, for example, is not considered net investment income. Neither is a return of capital. Therefore, managed distributions consisting of capital gains and/or return of capital do not result in a higher yield or a high yield fund.

**Question 13: Will additional information be available to shareholders?**

Yes. Current information about the Managed Distribution Plan will be included in the Fund’s quarterly reports to shareholders and will be posted on the Fund’s website, http://www.dnpselectincome.com. Through these channels, shareholders will be kept informed of any decision by the SEC regarding the Fund’s request for an exemptive order and any actions taken by the Board of Directors to modify, suspend or terminate the Plan.