

HOLLY ENERGY PARTNERS LP  
Form 10-Q  
November 05, 2015

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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

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FORM 10-Q

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(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT  
OF 1934

For the quarterly period ended September 30, 2015

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT  
OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: 1-32225

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HOLLY ENERGY PARTNERS, L.P.  
(Exact name of registrant as specified in its charter)

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Delaware (State or other jurisdiction of incorporation or organization)	20-0833098 (I.R.S. Employer Identification No.)
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2828 N. Harwood, Suite 1300 Dallas, Texas (Address of principal executive offices) (214) 871-3555 (Registrant's telephone number, including area code)	75201 (Zip code)
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(Former name, former address and former fiscal year, if changed since last report)

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Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

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Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined by Rule 12b-2 of the Exchange Act). Yes  No

The number of the registrant's outstanding common units at October 30, 2015 was 58,657,048.

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FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains certain “forward-looking statements” within the meaning of the federal securities laws. All statements, other than statements of historical fact included in this Form 10-Q, including, but not limited to, those under “Results of Operations” and “Liquidity and Capital Resources” in Item 2 “Management’s Discussion and Analysis of Financial Condition and Results of Operations” in Part I are forward-looking statements.

Forward-looking statements use words such as “anticipate,” “project,” “expect,” “plan,” “goal,” “forecast,” “intend,” “should,” “could,” “believe,” “may,” and similar expressions and statements regarding our plans and objectives for future operations.

These statements are based on our beliefs and assumptions and those of our general partner using currently available information and expectations as of the date hereof, are not guarantees of future performance and involve certain risks and uncertainties. Although we and our general partner believe that such expectations reflected in such forward-looking statements are reasonable, neither we nor our general partner can give assurance that our expectations will prove to be correct. All statements concerning our expectations for future results of operations are based on forecasts for our existing operations and do not include the potential impact of any future acquisitions. Our forward-looking statements are subject to a variety of risks, uncertainties and assumptions. If one or more of these risks or uncertainties materialize, or if underlying assumptions prove incorrect, our actual results may vary materially from those anticipated, estimated, projected or expected. Certain factors could cause actual results to differ materially from results anticipated in the forward-looking statements. These factors include, but are not limited to:

- risks and uncertainties with respect to the actual quantities of petroleum products and crude oil shipped on our pipelines and/or terminalled, stored or throughput in our terminals;
- the economic viability of HollyFrontier Corporation, Alon USA, Inc. and our other customers;
- the demand for refined petroleum products in markets we serve;
- our ability to purchase and integrate future acquired operations;
- our ability to complete previously announced or contemplated acquisitions;
- the availability and cost of additional debt and equity financing;
- the possibility of reductions in production or shutdowns at refineries utilizing our pipeline and terminal facilities;
- the effects of current and future government regulations and policies;
- our operational efficiency in carrying out routine operations and capital construction projects;
- the possibility of terrorist attacks and the consequences of any such attacks;
- general economic conditions; and
- other financial, operational and legal risks and uncertainties detailed from time to time in our Securities and Exchange Commission filings.

Cautionary statements identifying important factors that could cause actual results to differ materially from our expectations are set forth in this Form 10-Q, including without limitation, the forward-looking statements that are referred to above. When considering forward-looking statements, you should keep in mind the known material risk factors and other cautionary statements set forth in our Annual Report on Form 10-K for the year ended December 31, 2014, in our Quarterly Report on Form 10-Q for the quarter ended June 30, 2015, and in this Form 10-Q in “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and in “Risk Factors.” All forward-looking statements included in this Form 10-Q and all subsequent written or oral forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by these cautionary statements. The forward-looking statements speak only as of the date made and, other than as required by law, we undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

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## PART I. FINANCIAL INFORMATION

## Item 1. Financial Statements

HOLLY ENERGY PARTNERS, L.P.  
CONSOLIDATED BALANCE SHEETS

(in thousands, except unit data)

	September 30, 2015 (Unaudited)	December 31, 2014
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$10,856	\$2,830
Accounts receivable:		
Trade	7,867	6,737
Affiliates	26,101	33,392
	33,968	40,129
Prepaid and other current assets	4,573	4,383
Total current assets	49,397	47,342
Properties and equipment, net	990,567	980,479
Transportation agreements, net	75,542	80,703
Goodwill	256,498	256,498
Equity method investments	79,378	24,478
Other assets	14,647	12,055
Total assets	\$1,466,029	\$1,401,555
<b>LIABILITIES AND PARTNERS' EQUITY</b>		
Current liabilities:		
Accounts payable:		
Trade	\$7,522	\$12,642
Affiliates	3,714	5,239
	11,236	17,881
Accrued interest	1,851	6,615
Deferred revenue	11,674	12,432
Accrued property taxes	6,477	2,703
Other current liabilities	4,302	4,571
Total current liabilities	35,540	44,202
Long-term debt	951,067	867,579
Other long-term liabilities	21,532	18,145
Deferred revenue	37,242	29,392
Class B unit	32,107	26,793
Equity:		
Partners' equity:		

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Common unitholders (58,657,048 units issued and outstanding at September 30, 2015 and December 31, 2014)	434,210	468,813
General partner interest (2% interest)	(139,579	) (148,405 )
Accumulated other comprehensive loss	(834	) (46 )
Total partners' equity	293,797	320,362
Noncontrolling interest	94,744	95,082
Total equity	388,541	415,444
Total liabilities and equity	\$1,466,029	\$1,401,555

See accompanying notes.

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HOLLY ENERGY PARTNERS, L.P.  
CONSOLIDATED STATEMENTS OF INCOME  
(Unaudited)  
(In thousands, except per unit data)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Revenues:				
Affiliates	\$73,716	\$67,450	\$214,268	\$203,762
Third parties	14,673	14,680	47,356	40,370
	88,389	82,130	261,624	244,132
Operating costs and expenses:				
Operations (exclusive of depreciation and amortization)	24,095	25,456	77,350	72,835
Depreciation and amortization	16,326	15,483	46,083	46,953
General and administrative	3,673	2,266	9,659	7,933
	44,094	43,205	133,092	127,721
Operating income	44,295	38,925	128,532	116,411
Other income (expense):				
Equity in earnings of equity method investments	1,269	880	2,634	2,150
Interest expense	(9,486)	(8,585)	(27,310)	(27,368)
Interest income	381	—	384	3
Loss on early extinguishment of debt	—	—	—	(7,677)
Other expense	176	11	406	45
	(7,660)	(7,694)	(23,886)	(32,847)
Income before income taxes	36,635	31,231	104,646	83,564
State income tax expense	(69)	(42)	(106)	(145)
Net income	36,566	31,189	104,540	83,419
Allocation of net income attributable to noncontrolling interests	(2,081)	(1,509)	(7,851)	(6,562)
Net income attributable to Holly Energy Partners	34,485	29,680	96,689	76,857
General partner interest in net income, including incentive distributions	(10,830)	(8,940)	(30,835)	(25,334)
Limited partners' interest in net income	\$23,655	\$20,740	\$65,854	\$51,523
Limited partners' per unit interest in earnings—basic and diluted	\$0.40	\$0.35	\$1.11	\$0.87
Weighted average limited partners' units outstanding	58,657	58,657	58,657	58,657

See accompanying notes.

HOLLY ENERGY PARTNERS, L.P.  
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME  
(Unaudited)  
(In thousands)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Net income	\$36,566	\$31,189	\$104,540	\$83,419
Other comprehensive income:				
Change in fair value of cash flow hedging instruments	(787	) 553	(2,373	) (1,189
Reclassification adjustment to net income on partial settlement of cash flow hedge	526	556	1,585	1,647
Other comprehensive income (loss)	(261	) 1,109	(788	) 458
Comprehensive income before noncontrolling interest	36,305	32,298	103,752	83,877
Allocation of comprehensive income to noncontrolling interests	(2,081	) (1,509	) (7,851	) (6,562
Comprehensive income attributable to Holly Energy Partners	\$34,224	\$30,789	\$95,901	\$77,315

See accompanying notes.



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HOLLY ENERGY PARTNERS, L.P.  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(Unaudited)  
(In thousands)

	Nine Months Ended September 30,	
	2015	2014
Cash flows from operating activities		
Net income	\$ 104,540	\$ 83,419
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	46,083	46,953
Gain on sale of assets	(351)	) —
Amortization of deferred charges	1,425	1,384
Amortization of restricted and performance units	3,023	2,493
Distributions less than income from equity investments	(416)	) —
Loss on early extinguishment of debt	—	7,677
(Increase) decrease in operating assets:		
Accounts receivable—trade	(1,094)	) (700)
Accounts receivable—affiliates	7,800	(536)
Prepaid and other current assets	(146)	) (545)
Increase (decrease) in operating liabilities:		
Accounts payable—trade	(2,943)	) 608
Accounts payable—affiliates	(1,525)	) (4,191)
Accrued interest	(4,764)	) (8,417)
Deferred revenue	7,092	5,051
Accrued property taxes	3,774	3,867
Other current liabilities	(365)	) 467
Other, net	3,773	(877)
Net cash provided by operating activities	165,906	136,653
Cash flows from investing activities		
Additions to properties and equipment	(30,923)	) (58,313)
Purchase of El Dorado crude tanks	(27,500)	) —
Purchase of investment in Frontier Pipeline	(54,641)	) —
Proceeds from sale of assets	1,244	—
Distributions in excess of equity in earnings of equity investments	158	163
Net cash used for investing activities	(111,662)	) (58,150)
Cash flows from financing activities		
Borrowings under credit agreement	443,000	538,600
Repayments of credit agreement borrowings	(360,000)	) (346,600)
Redemption of senior notes	—	(156,188)
Distributions to HEP unitholders	(125,242)	) (114,680)
Distributions to noncontrolling interest	(2,875)	) (3,250)
Purchase of units for incentive grants	(247)	) (1,064)
Other	(854)	) (6)
Net cash used by financing activities	(46,218)	) (83,188)

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Cash and cash equivalents			
Increase (decrease) for the period	8,026	(4,685	)
Beginning of period	2,830	6,352	
End of period	\$ 10,856	\$ 1,667	

See accompanying notes.

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HOLLY ENERGY PARTNERS, L.P.  
CONSOLIDATED STATEMENTS OF PARTNERS' EQUITY  
(Unaudited)  
(In thousands)

	Common Units	General Partner Interest	Accumulated Other Comprehensive Loss	Noncontrolling Interest	Total Equity
Balance December 31, 2014	\$468,813	\$(148,405 )	\$(46 )	\$95,082	\$415,444
Distributions to HEP unitholders	(94,579 )	(30,663 )	—	—	(125,242 )
Distributions to noncontrolling interest	—	—	—	(2,875 )	(2,875 )
Purchase of units for incentive grants	(247 )	—	—	—	(247 )
Amortization of restricted and performance units	3,023	—	—	—	3,023
Class B unit accretion	(5,208 )	(106 )	—	—	(5,314 )
Net income	62,408	39,595	—	2,537	104,540
Other comprehensive loss	—	—	(788 )	—	(788 )
Balance September 30, 2015	\$434,210	\$(139,579 )	\$(834 )	\$94,744	\$388,541

See accompanying notes.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 1: Description of Business and Presentation of Financial Statements

Holly Energy Partners, L.P. ("HEP"), together with its consolidated subsidiaries, is a publicly held master limited partnership which is 39% owned (including the 2% general partner interest) by HollyFrontier Corporation ("HFC") and its subsidiaries. We commenced operations on July 13, 2004, upon the completion of our initial public offering. In these consolidated financial statements, the words "we," "our," "ours" and "us" refer to HEP unless the context otherwise indicates.

We operate in one reportable segment which represents the aggregation of our petroleum product and crude pipelines business and terminals, tankage and loading rack facilities operation.

We own and operate petroleum product and crude oil pipelines and terminal, tankage and loading rack facilities that support HFC's refining and marketing operations in the Mid-Continent, Southwest and Rocky Mountain regions of the United States and Alon USA, Inc.'s ("Alon") refinery in Big Spring, Texas. Additionally, we own a 75% interest in UNEV Pipeline, LLC ("UNEV"), which owns a 427-mile, 12-inch refined products pipeline running from Woods Cross, Utah to Las Vegas, Nevada (the "UNEV Pipeline"), product terminals near Cedar City, Utah and Las Vegas, Nevada and related assets, and a 25% interest in SLC Pipeline LLC, which owns a 95-mile intrastate crude oil pipeline system (the "SLC Pipeline") that serves refineries in the Salt Lake City, Utah area.

We generate revenues by charging tariffs for transporting petroleum products and crude oil through our pipelines, by charging fees for terminalling and storing refined products and other hydrocarbons, and providing other services at our storage tanks and terminals. We do not take ownership of products that we transport, terminal or store, and therefore, we are not exposed directly to changes in commodity prices.

The consolidated financial statements included herein have been prepared without audit, pursuant to the rules and regulations of the United States Securities and Exchange Commission (the "SEC"). The interim financial statements reflect all adjustments, which, in the opinion of management, are necessary for a fair presentation of our results for the interim periods. Such adjustments are considered to be of a normal recurring nature. Although certain notes and other information required by U.S. generally accepted accounting principles ("GAAP") have been condensed or omitted, we believe that the disclosures in these consolidated financial statements are adequate to make the information presented not misleading. These consolidated financial statements should be read in conjunction with our Annual Report on Form 10-K for the year ended December 31, 2014. Results of operations for interim periods are not necessarily indicative of the results of operations that will be realized for the year ending December 31, 2015.

Acquisitions

On August 31, 2015, we purchased a 50% interest in Frontier Pipeline Company, which owns a 289-mile crude oil pipeline running from Casper, Wyoming to Frontier Station, Utah (the "Frontier Pipeline"), from an affiliate of Enbridge, Inc. for cash consideration of \$54.6 million. Frontier Pipeline will continue to be operated by an affiliate of Plains All American Pipeline, L.P., which owns the remaining 50% interest. The Frontier Pipeline has a 72,000 barrel per day ("bpd") capacity and supplies Canadian and Rocky Mountain crudes to Salt Lake City area refiners through a connection to the SLC Pipeline.

On November 1, 2015, we acquired from Frontier El Dorado Refining LLC, a wholly owned subsidiary of HFC, all the outstanding membership interests in El Dorado Operating LLC ("El Dorado Operating"), which owns the newly constructed naphtha fractionation and hydrogen generation units at HFC's El Dorado refinery for cash consideration of

\$62.0 million. In connection with this transaction, we entered into 15-year tolling agreements containing minimum quarterly throughput commitments from HFC that provide minimum annualized revenues of \$15.3 million.

We are a consolidated variable interest entity of HFC. Therefore, this transaction will be recorded as a transfer between entities under common control and reflect HFC's carrying basis in El Dorado Operating's assets and liabilities. Also, we will retrospectively adjust our financial position and operating results as if El Dorado Operating were a consolidated subsidiary for all periods while we were under common control of HFC. Assuming this acquisition was effective as of September 30, 2015, our assets, liabilities and partners' equity would have been retrospectively adjusted to include El Dorado Operating's assets, liabilities and partners' equity as presented below:

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HOLLY ENERGY PARTNERS, L.P.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited) Continued

	September 30, 2015 (In thousands)	December 31, 2014
Properties and equipment, net	\$60,320	