

PHILLIPS 66 PARTNERS LP  
Form S-3  
March 01, 2016  
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As filed with the Securities and Exchange Commission on March 1, 2016

Registration No. 333-

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

FORM S-3  
REGISTRATION STATEMENT  
*UNDER*  
*THE SECURITIES ACT OF 1933*

**Phillips 66 Partners LP**  
(Exact name of registrant as specified in its charter)

Delaware  
(State or other jurisdiction of  
incorporation or organization)

3010 Briarpark Drive

38-3899432  
(I.R.S. Employer  
Identification No.)

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**Houston, Texas 77042**

**(855) 283-9237**

**(Address, including zip code, and telephone number, including area code, of registrant's principal executive offices)**

**Paula A. Johnson**

**Vice President, General Counsel and Secretary**

**3010 Briarpark Drive**

**Houston, Texas 77042**

**(855) 283-9237**

**(Name, address, including zip code, and telephone number, including area code, of agent for service)**

*Copy to:*

**Brett E. Braden**

**Thomas G. Brandt**

**Latham & Watkins LLP**

**811 Main Street, Suite 3700**

**Houston, Texas 77002**

**(713) 546-5400**

Approximate date of commencement of proposed sale to the public:

**From time to time after the effective date of this Registration Statement.**

If the only securities being registered on this Form are to be offered pursuant to dividend or interest reinvestment plans, please check the following box. "

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If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, as amended, other than securities offered only in connection with dividend or interest reinvestment plans, check the following box.

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If this Form is a registration statement pursuant to General Instruction I.D. or a post-effective amendment thereto that shall become effective upon filing with the Commission pursuant to Rule 462(e) under the Securities Act, check the following box.

If this Form is a post-effective amendment to a registration statement filed pursuant to General Instruction I.D. filed to register additional securities or additional classes of securities pursuant to Rule 413(b) under the Securities Act, check the following box.

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. (Check one):

Large accelerated filer  Accelerated filer   
 Non-accelerated filer  (Do not check if a smaller reporting company) Smaller reporting company

**CALCULATION OF REGISTRATION FEE**

Title of Each Class of Securities to be Registered	Proposed Maximum Aggregate Offering Price(1)	Amount of Registration Fee(2)
Common units representing limited partner interests	\$250,000,000	\$25,175

(1) An indeterminate number of common units representing limited partner interests in Phillips 66 Partners LP, may be issued from time to time at indeterminate prices, with an aggregate offering price not to exceed \$250,000,000.

(2) Calculated in accordance with Rule 457(o) under the Securities Act and paid herewith.

**The Registrant hereby amends this Registration Statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment which specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933 or until this Registration Statement shall become effective on such date as the Securities and Exchange Commission, acting pursuant to said Section 8(a), may determine.**

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**The information in this prospectus is not complete and may be changed. The securities may not be sold until the registration statement filed with the Securities and Exchange Commission is effective. This prospectus is not an offer to sell these securities and it is not soliciting an offer to buy these securities in any state where the offer or sale is not permitted.**

**SUBJECT TO COMPLETION, DATED MARCH 1, 2016**

**PROSPECTUS**

**\$250,000,000**

**Phillips 66 Partners LP**

**Common Units Representing Limited Partner Interests**

We may offer and sell up to \$250,000,000 in aggregate offering price of common units representing limited partner interests in Phillips 66 Partners LP from time to time in amounts, at prices and on terms to be determined by market conditions and other factors at the time of our offerings.

We may offer and sell the common units to or through one or more underwriters, dealers or agents, or directly to purchasers, on a continuous or delayed basis. This prospectus describes the terms of the common units and the general manner in which we will offer the common units. The specific manner in which we will offer the common units and arrangements with any underwriters, dealers or agents will be included in the prospectus supplement that relates to that offering.

Our common units are traded on the New York Stock Exchange, or the NYSE, under the symbol PSXP.

**Investing in our common units involves risks. You should carefully consider the factors described under Risk Factors beginning on page 2 of this prospectus and any similar section contained in the applicable prospectus supplement before you make an investment in our common units.**

**Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.**

**The date of this prospectus is \_\_\_\_\_, 2016.**

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**In making your investment decision, you should rely only on the information contained or incorporated by reference in this prospectus. We have not authorized anyone to provide you with any other information. If anyone provides you with different or inconsistent information, you should not rely on it.**

**You should not assume that the information contained in this prospectus is accurate as of any date other than the date on the front cover of this prospectus. You should not assume that the information contained in the documents incorporated by reference in this prospectus is accurate as of any date other than the respective dates of those documents. Our business, financial condition, results of operations and prospects may have changed since those dates.**

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**ABOUT THIS PROSPECTUS**

This prospectus is part of a registration statement on Form S-3 that we have filed with the Securities and Exchange Commission, or the SEC, under the Securities Act of 1933, as amended, or the Securities Act, utilizing a shelf registration process. Under this shelf registration process, we may, from time to time, sell up to \$250,000,000 of our common units in one or more offerings.

This prospectus provides you with a general description of Phillips 66 Partners LP and the common units that are registered hereunder that may be offered by us. Each time we sell any common units offered by this prospectus, we will provide a prospectus supplement that will contain specific information about the terms of that offering and the common units being offered. To the extent information in this prospectus is inconsistent with the information contained in a prospectus supplement, you should rely on the information in the prospectus supplement.

A prospectus supplement may include additional risk factors or other special considerations applicable to those common units and may also add, update or change information in this prospectus. Additional information, including our financial statements and the notes thereto, is incorporated in this prospectus by reference to our reports filed with the SEC. Please read **Where You Can Find More Information**. You are urged to read carefully this prospectus and any prospectus supplement relating to the common units offered to you, together with the additional information described under the heading **Where You Can Find More Information**, before investing in our common units.

Unless the context otherwise requires, references in this prospectus to **Phillips 66 Partners LP**, **the Partnership**, **we**, **our**, **us**, or like terms refer to Phillips 66 Partners LP and our subsidiaries. **Phillips 66** refers to Phillips 66 and its consolidated subsidiaries, other than Phillips 66 Partners LP, our subsidiaries and our general partner. References to **our general partner** refer to Phillips 66 Partners GP LLC.



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**WHERE YOU CAN FIND MORE INFORMATION**

We have filed a registration statement with the SEC under the Securities Act that registers the common units offered by this prospectus. The registration statement, including the attached exhibits, contains additional relevant information about us. The rules and regulations of the SEC allow us to omit some information included in the registration statement from this prospectus.

The SEC allows us to incorporate by reference the information we have filed with the SEC. This means that we can disclose important information to you without actually including the specific information in this prospectus by referring you to other documents filed separately with the SEC. These other documents contain important information about us, our financial condition and our results of operations. The information incorporated by reference is an important part of this prospectus. Information that we file later with the SEC will automatically update and may replace information in this prospectus and information previously filed with the SEC.

We incorporate by reference the documents listed below and any future filings we make with the SEC under Sections 13(a), 13(c), 14 or 15(d) of the Securities Exchange Act of 1934, as amended, or the Exchange Act, excluding any information in those documents that is deemed by the rules of the SEC to be furnished not filed, until the termination of the registration statement:

our annual report on Form 10-K for the year ended December 31, 2015, which was filed with the SEC on February 12, 2016;

our current reports on Form 8-K as filed with the SEC on February 17, 2015, February 18, 2016, and March 1, 2016 (excluding any information furnished pursuant to Item 2.02 or Item 7.01 of any such Current Report on Form 8-K); and

the description of our common units contained in our registration statement on Form 8-A (File No. 001-36011) filed with the SEC on July 18, 2013, and including any other amendments or reports filed for the purpose of updating such description.

Our principal executive offices are located at 3010 Briarpark Drive, Houston, Texas 77042, and our telephone number is (855) 283-9237. Our common units trade on the New York Stock Exchange under the symbol PSXP. We file annual, quarterly and other reports and other information with the SEC. You may read and copy any document that we file with the SEC at the SEC's Public Reference Room at 100 F Street, N.E., Washington, DC 20549. You may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. Our SEC filings are also available to the public on the SEC's website at <http://www.sec.gov>. We also make available, free of charge on our website at <http://www.phillips66partners.com>, all materials that we electronically file with the SEC, including our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, Section 16 reports, and amendments to these reports as soon as reasonably practicable after we electronically file such material with, or furnish it to, the SEC. The information on our website, however, is not, and should not be deemed to be, a part of this prospectus. You may request a copy of any document incorporated by reference in this prospectus (including exhibits to those documents specifically incorporated by reference in this prospectus), free of charge, by contacting us at Phillips 66 Partners LP, Attention: Investor Relations, 3010 Briarpark Drive, Houston, Texas 77042, (855) 283-9237, or [investorrelations@p66partners.com](mailto:investorrelations@p66partners.com). We also post on our website our governance guidelines, code of business ethics and conduct, and the charter for the audit committee of our board of directors.



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**FORWARD-LOOKING STATEMENTS**

Some of the statements and information included in this prospectus, any prospectus supplement and the information incorporated by reference in this prospectus or any prospectus supplement may contain forward-looking statements. You can identify our forward-looking statements by the words anticipate, estimate, believe, budget, continue, intend, may, plan, potential, predict, seek, should, will, would, expect, objective, projection, outlook, effort, target and similar expressions.

We based the forward-looking statements on our current expectations, estimates and projections about us and the industries in which we operate in general. We caution you these statements are not guarantees of future performance as they involve assumptions that, while made in good faith, may prove to be incorrect, and involve risks and uncertainties we cannot predict. In addition, we based many of these forward-looking statements on assumptions about future events that may prove to be inaccurate. Accordingly, our actual outcomes and results may differ materially from what we have expressed or forecast in the forward-looking statements. Any differences could result from a variety of factors, including the following:

the continued ability of Phillips 66 to satisfy its obligations under our commercial and other agreements;

the volume of crude oil, natural gas liquids, or NGL, and refined petroleum products we transport, fractionate, terminal and store;

the tariff rates with respect to volumes that we transport through our regulated assets, which rates are subject to review and possible adjustment by federal and state regulators;

changes in revenue we realize under the loss allowance provisions of our regulated tariffs resulting from changes in underlying commodity prices;

fluctuations in the prices for crude oil, NGL and refined petroleum products;

changes in global economic conditions and the effects of a global economic downturn on the business of Phillips 66 and the business of its suppliers, customers, business partners and credit lenders;

liabilities associated with the risks and operational hazards inherent in transporting, fractionating, terminaling and storing crude oil, NGL and refined petroleum products;

curtailment of operations due to severe weather disruption; riots, strikes, lockouts or other industrial disturbances; or failure of information technology systems due to various causes, including unauthorized access or attack;

inability to timely obtain or maintain permits, including those necessary for capital projects; comply with government regulations; or make capital expenditures required to maintain compliance;

failure to timely complete construction of announced and future capital projects;

the operation, financing and distribution decisions of our joint ventures;

costs or liabilities associated with federal, state, and local laws and regulations relating to environmental protection and safety, including spills, releases and pipeline integrity;

costs associated with compliance with evolving environmental laws and regulations on climate change;

costs associated with compliance with safety regulations, including pipeline integrity management program testing and related repairs;

changes in the cost or availability of third-party vessels, pipelines, rail cars and other means of delivering and transporting crude oil, NGL and refined petroleum products; and

direct or indirect effects on our business resulting from actual or threatened terrorist incidents or acts of war.

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When considering forward-looking statements, you should keep in mind the risk factors and other cautionary statements set forth in this prospectus and any prospectus supplement, as well as other written and oral statements made or incorporated by reference from time to time by us in other reports and filings with the SEC. All forward-looking statements included in this prospectus, any prospectus supplement 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, other than as required by law, and 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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**ABOUT PHILLIPS 66 PARTNERS LP**

We are a growth-oriented master limited partnership formed in 2013 by Phillips 66 to own, operate, develop and acquire primarily fee-based crude oil, refined petroleum product and NGL pipelines and terminals and other transportation and midstream assets. Our assets consist of one crude oil pipeline, terminal and storage system; four refined petroleum products pipeline, terminal and storage systems; two crude oil rail racks; two refinery-grade propylene storage spheres; one crude oil gathering system; and interests in seven joint ventures. The majority of our assets are connected to, and integral to the operation of, seven of Phillips 66's wholly owned or jointly owned refineries.

We generate revenue primarily by charging tariffs and fees for transporting crude oil and refined petroleum products through our pipelines, and for terminaling and storing crude oil, NGL and refined petroleum products at our terminals, rail racks and storage facilities. In addition, our joint ventures generate revenue primarily from transporting crude oil, NGL and refined petroleum products and fractionating and storing NGL. Because we do not own any of the crude oil and refined petroleum products we handle and do not engage in the trading of crude oil and refined petroleum products, we have limited direct exposure to risks associated with fluctuating commodity prices, although these risks indirectly influence our activities and results of operations over the long term.

We have multiple commercial agreements with Phillips 66, including transportation services agreements, terminal services agreements, storage services agreements, stevedoring services agreements, a fractionation agreement and rail terminal services agreements. Under these long-term, fee-based agreements, we provide transportation, terminaling, storage, stevedoring, fractionation and rail terminal services to Phillips 66, and Phillips 66 commits to provide us with minimum throughput volumes of crude oil, NGL and refined petroleum products or minimum monthly capacity or service fees.

Our general partner, Phillips 66 Partners GP LLC, is a Delaware limited liability company. We are managed and controlled by our general partner.

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**RISK FACTORS**

An investment in our common units involves risks. Before you invest in our common units, you should carefully consider the risk factors included in our most recent annual report on Form 10-K, subsequent quarterly reports on Form 10-Q, current reports on Form 8-K and those that may be included in any applicable prospectus supplement, as well as risks described in Management's Discussion and Analysis of Financial Condition and Results of Operations and cautionary notes regarding forward-looking statements included or incorporated by reference in this prospectus, together with all of the other information included or incorporated by reference in this prospectus, any prospectus supplement and the documents we incorporate by reference.

If any of these risks were to materialize, our business, results of operations, cash flows and financial condition could be materially adversely affected. In that case, our ability to make distributions to our unitholders may be reduced, the trading price of our common units could decline and you could lose all or part of your investment.

**USE OF PROCEEDS**

Unless otherwise indicated to the contrary in an applicable prospectus supplement, we will use the net proceeds from the sale of the common units covered by this prospectus for general partnership purposes, which may include debt repayment, future acquisitions, capital expenditures and additions to working capital.

Any allocation of the net proceeds of an offering of common units to a specific purpose will be determined at the time of the offering and will be described in a prospectus supplement.

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**DESCRIPTION OF OUR COMMON UNITS**

The following description of our common units is not complete and may not contain all the information you should consider before investing in our common units. This description is summarized from, and qualified in its entirety by reference to, our partnership agreement, which has been publicly filed with the SEC. See [Where You Can Find More Information](#).

**The Common Units**

The common units represent limited partner interests in us. The holders of common units are entitled to participate in partnership distributions and exercise the rights or privileges available to limited partners under our partnership agreement. For a description of the rights and preferences of holders of common units in and to partnership distributions, please read this section and [Provisions of Our Partnership Agreement Relating to Cash Distributions](#). For a description of the rights and privileges of limited partners under our partnership agreement, including voting rights, please read [Our Partnership Agreement](#). Our outstanding common units are listed on the NYSE under the symbol [PSXP](#) and any additional common units we issue will also be listed on the NYSE. As of February 28, 2016, 82,487,792 common units were outstanding.

**Transfer Agent and Registrar**

***Duties***

American Stock Transfer & Trust Company, LLC serves as registrar and transfer agent for our common units. We pay all fees charged by the transfer agent for transfers of common units, except for the following, which must be paid by unitholders:

surety bond premiums to replace lost or stolen certificates, or to cover related taxes and other governmental charges;

special charges for services requested by a holder of a common unit; and

other similar fees or charges.

There is no charge to unitholders for disbursements of our cash distributions. We will indemnify the transfer agent, its agents and each of their stockholders, directors, officers and employees against all claims and losses that may arise out of acts performed or omitted for its activities in that capacity, except for any liability due to any gross negligence or intentional misconduct of the indemnified person or entity.

***Resignation or Removal***

The transfer agent may resign, by notice to us, or be removed by us. The resignation or removal of the transfer agent will become effective upon our appointment of a successor transfer agent and registrar and its acceptance of the appointment. If no successor has been appointed and has accepted the appointment within 30 days after notice of the resignation or removal, our general partner may act as the transfer agent and registrar until a successor is appointed.



**Transfer of Common Units**

Upon the transfer of a common unit in accordance with our partnership agreement, each transferee of common units shall be admitted as a limited partner with respect to the common units transferred when such transfer and admission are reflected in our books and records. Each transferee:

automatically agrees to be bound by the terms and conditions of, and is deemed to have executed, our partnership agreement;

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represents and warrants that the transferee has the right, power, authority, and capacity to enter into our partnership agreement; and

gives the consents, waivers and approvals contained in our partnership agreement.

Our general partner will cause any transfers to be recorded on our books and records no less frequently than quarterly.

We may, at our discretion, treat the nominee holder of a common unit as the absolute owner. In that case, the beneficial holder's rights are limited solely to those that it has against the nominee holder as a result of any agreement between the beneficial owner and the nominee holder.

Common units are securities and any transfers are subject to the laws governing the transfer of securities. In addition to other rights acquired upon transfer, the transferor gives the transferee the right to become a substituted limited partner in our partnership for the transferred common units.

Until a common unit has been transferred on our books, we and the transfer agent may treat the record holder of the common unit as the absolute owner for all purposes, except as otherwise required by law or stock exchange regulations.

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**PROVISIONS OF OUR PARTNERSHIP AGREEMENT RELATING TO CASH DISTRIBUTIONS**

Set forth below is a summary of the significant provisions of our partnership agreement that relate to cash distributions.

**Distributions of Available Cash**

*General*

Our partnership agreement requires that, within 45 days after the end of each quarter, we distribute all of our available cash to unitholders of record on the applicable record date.

*Definition of available cash*

Available cash generally means, for any quarter, all cash and cash equivalents on hand at the end of that quarter:

*less*, the amount of cash reserves established by our general partner to:

provide for the proper conduct of our business (including reserves for our future capital expenditures, future acquisitions, anticipated future debt service requirements and refunds of collected rates reasonably likely to be refunded as a result of a settlement or hearing related to FERC rate proceedings or rate proceedings under applicable law) subsequent to that quarter;

comply with applicable law, any of our or our subsidiaries' debt instruments or other agreements; or

provide funds for distributions to our unitholders and to our general partner for any one or more of the next four quarters (provided that our general partner may not establish cash reserves for distributions if the effect of the establishment of such reserves will prevent us from distributing the minimum quarterly distribution on all common units and any cumulative arrearages on such common units for the current quarter);

*plus*, if our general partner so determines, all or any portion of the cash on hand on the date of determination of available cash for the quarter resulting from working capital borrowings made subsequent to the end of such quarter.

The purpose and effect of the last bullet point above is to allow our general partner, if it so decides, to use cash from working capital borrowings made after the end of the quarter but on or before the date of determination of available cash for that quarter to pay distributions to unitholders. Under our partnership agreement, working capital borrowings are generally borrowings that are made under a credit facility, commercial paper facility or similar financing arrangement, and in all cases are used solely for working capital purposes or to pay distributions to partners and with the intent of the borrower to repay such borrowings within 12 months with funds other than from additional working capital borrowings.

***Intent to distribute the minimum quarterly distribution***

We intend to make at least the minimum quarterly distribution to the holders of our common units of \$0.2125 per unit, or \$0.85 per unit on an annualized basis, to the extent we have sufficient available cash after the establishment of cash reserves. Our most recent quarterly distribution declared by the board of directors of our general partner, which was for the three months ended December 31, 2015, was \$0.458 per unit, or \$1.832 per unit on an annualized basis. However, there is no guarantee that we will pay the minimum quarterly distribution on our units in any quarter. The amount of distributions paid under our cash distribution policy and the decision to make any distribution will be determined by our general partner in accordance with our partnership agreement.

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### ***General partner interest and incentive distribution rights***

As of the date of this prospectus, our general partner is entitled to 2% of all quarterly distributions that we make prior to our liquidation. Our general partner has the right, but not the obligation, to contribute a proportionate amount of capital to us to maintain its current general partner interest. The general partner interest in these distributions will be reduced if we issue additional units in the future and our general partner does not contribute a proportionate amount of capital to us to maintain its 2% general partner interest.

Our general partner also currently holds incentive distribution rights that entitle it to receive increasing percentages, up to a maximum of 48%, of the available cash we distribute from operating surplus (as defined below) in excess of \$0.244375 per unit per quarter. The maximum distribution of 48% does not include any distributions that our general partner or its affiliates may receive on common units or general partner units that they own. Please read [General Partner Interest and Incentive Distribution Rights](#) for additional information.

### **Operating Surplus and Capital Surplus**

#### ***General***

All cash distributed to unitholders will be characterized as either being paid from [operating surplus](#) or [capital surplus](#). We treat distributions of available cash from operating surplus differently than distributions of available cash from capital surplus.

#### ***Operating surplus***

We define operating surplus as:

\$60.0 million (as described below); *plus*

all of our cash receipts, excluding cash from interim capital transactions (as defined below) and the termination of commodity hedge or interest rate hedge contracts, provided that cash receipts from the termination of a commodity hedge or interest rate hedge prior to its specified termination date shall be included in operating surplus in equal quarterly installments over the remaining scheduled life of such commodity hedge or interest rate hedge; *plus*

working capital borrowings made after the end of a quarter but on or before the date of determination of operating surplus for that quarter; *plus*

cash distributions (including incremental distributions on incentive distribution rights) paid in respect of equity issued to finance all or a portion of expansion capital expenditures in respect of the period from the date that we enter into a binding obligation to commence the construction, development, replacement, improvement or expansion of a capital asset and ending on the earlier to occur of the date the capital asset commences commercial service and the date that it is abandoned or disposed of; *less*

all of our operating expenditures (as defined below); *less*

the amount of cash reserves established by our general partner to provide funds for future operating expenditures; *less*

all working capital borrowings not repaid within twelve months after having been incurred, or repaid within such 12-month period with the proceeds of additional working capital borrowings.

As described above, operating surplus does not reflect actual cash on hand that is available for distribution to our unitholders and is not limited to cash generated by operations. For example, it includes a provision that will enable us, if we choose, to distribute as operating surplus up to \$60.0 million of cash we receive in the future from non-operating sources such as asset sales, issuances of securities and long-term borrowings that would otherwise be distributed as capital surplus. In addition, the effect of including, as described above, certain cash distributions on equity interests in operating surplus will be to increase operating surplus by the amount of any such cash distributions. As a result, we may also distribute as operating surplus up to the amount of any such cash that we receive from non-operating sources.

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The proceeds of working capital borrowings increase operating surplus and repayments of working capital borrowings are generally operating expenditures (as described below) and thus reduce operating surplus when repayments are made. However, if working capital borrowings, which increase operating surplus, are not repaid during the twelve-month period following the borrowing, they will be deemed repaid at the end of such period, thus decreasing operating surplus at such time. When such working capital borrowings are in fact repaid, they will not be treated as a further reduction in operating surplus because operating surplus will have been previously reduced by the deemed repayment.

We define interim capital transactions as (1) borrowings, refinancings or refundings of indebtedness (other than working capital borrowings and items purchased on open account or for a deferred purchase price in the ordinary course of business) and sales of debt securities, (2) sales of equity securities, and (3) sales or other dispositions of assets, other than sales or other dispositions of inventory, accounts receivable and other assets in the ordinary course of business and sales or other dispositions of assets as part of normal asset retirements or replacements.

We define operating expenditures as all of our cash expenditures, including, but not limited to, taxes, reimbursements of expenses of our general partner and its affiliates, officer, director and employee compensation, debt service payments, payments made in the ordinary course of business under interest rate hedge contracts and commodity hedge contracts (provided that payments made in connection with the termination of any interest rate hedge contract or commodity hedge contract prior to the expiration of its settlement or termination date specified therein will be included in operating expenditures in equal quarterly installments over the remaining scheduled life of such interest rate hedge contract or commodity hedge contract and amounts paid in connection with the initial purchase of an interest rate hedge contract or a commodity hedge contract will be amortized over the life of such interest rate hedge contract or commodity hedge contract), maintenance capital expenditures (as discussed in further detail below), and repayment of working capital borrowings; provided, however, that operating expenditures will not include:

repayments of working capital borrowings where such borrowings have previously been deemed to have been repaid (as described above);

payments (including prepayments and prepayment penalties) of principal of and premium on indebtedness other than working capital borrowings;

expansion capital expenditures;

payment of transaction expenses (including taxes) relating to interim capital transactions;

distributions to our partners; or

repurchases of partnership interests (excluding repurchases we make to satisfy obligations under employee benefit plans).

***Capital surplus***

Capital surplus is defined in our partnership agreement as any distribution of available cash in excess of our cumulative operating surplus. Accordingly, except as described above, capital surplus would generally be generated by:

borrowings other than working capital borrowings;

sales of our equity and debt securities;

sales or other dispositions of assets, other than inventory, accounts receivable and other assets sold in the ordinary course of business or as part of ordinary course retirement or replacement of assets; and

capital contributions received.



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### ***Characterization of cash distributions***

All available cash distributed by us on any date from any source will be treated as distributed from operating surplus until the sum of all available cash distributed equals our cumulative operating surplus. We anticipate that distributions from operating surplus will generally not represent a return of capital. However, operating surplus, as defined in our partnership agreement, includes certain components, including a \$60.0 million cash basket, that represent non-operating sources of cash. Consequently, it is possible that all or a portion of specific distributions from operating surplus may represent a return of capital. Any available cash distributed by us in excess of our cumulative operating surplus will be deemed to be capital surplus under our partnership agreement. Our partnership agreement treats a distribution of capital surplus as the repayment of the initial unit price from our initial public offering and as a return of capital. We do not anticipate that we will make any distributions from capital surplus.

### **Capital Expenditures**

Maintenance capital expenditures are cash expenditures (including expenditures for the construction or development of new capital assets or the replacement, improvement or expansion of existing capital assets) made to maintain, over the long term, our operating capacity or operating income. Examples of maintenance capital expenditures are expenditures to repair, refurbish and replace pipelines and storage facilities, to maintain equipment reliability, integrity and safety and to address environmental laws and regulations.

Expansion capital expenditures are cash expenditures incurred for acquisitions or capital improvements that we expect will increase our operating capacity or operating income over the long term. Examples of expansion capital expenditures include the acquisition of equipment, or the construction, development or acquisition of additional pipeline or storage capacity, to the extent such capital expenditures are expected to expand our long-term operating capacity or operating income. Expansion capital expenditures include interest payments (and related fees) on debt incurred to finance all or a portion of expansion capital expenditures in respect of the period from the date that we enter into a binding obligation to commence the construction, development, replacement, improvement or expansion of a capital asset and ending on the earlier to occur of the date that such capital improvement commences commercial service and the date that such capital improvement is abandoned or disposed of.

Capital expenditures that are made in part for maintenance capital purposes and in part for expansion capital purposes will be allocated as maintenance capital expenditures or expansion capital expenditures by our general partner.

### **Distributions of Available Cash From Operating Surplus**

Assuming our general partner maintains its 2% general partner interest and we do not issue additional classes of equity securities, we will make distributions of available cash from operating surplus for any quarter in the following manner:

*first*, 98% to all unitholders, pro rata, and 2% to our general partner, until we distribute for each outstanding unit an amount equal to the minimum quarterly distribution for that quarter; and

*thereafter*, in the manner described in **General Partner Interest and Incentive Distribution Rights** below.

### **General Partner Interest and Incentive Distribution Rights**

Our partnership agreement provides that our general partner initially will be entitled to 2% of all distributions that we make prior to our liquidation. Our general partner has the right, but not the obligation, to contribute a proportionate amount of capital to us in order to maintain its 2% general partner interest if we issue additional units. Our general partner's 2% interest, and the percentage of our cash distributions to which it is entitled from such 2% interest, will be proportionately reduced if we issue additional units in the future (other

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than the issuance of common units upon a reset of the incentive distribution rights) and our general partner does not contribute a proportionate amount of capital to us in order to maintain its 2% general partner interest. Our partnership agreement does not require that our general partner fund its capital contribution with cash. Our general partner may instead fund its capital contribution by the contribution to us of common units or other property.

Incentive distribution rights represent the right to receive an increasing percentage (13%, 23% and 48%) of quarterly distributions of available cash from operating surplus after the minimum quarterly distribution and the target distribution levels have been achieved. Our general partner currently holds the incentive distribution rights, but may transfer these rights separately from its general partner interest.

The following discussion assumes that our general partner maintains its 2% general partner interest, and that our general partner continues to own the incentive distribution rights.

If for any quarter:

we have distributed available cash from operating surplus to the common unitholders in an amount equal to the minimum quarterly distribution; and

we have distributed available cash from operating surplus on outstanding common units in an amount necessary to eliminate any cumulative arrearages in payment of the minimum quarterly distribution; then, we will distribute any additional available cash from operating surplus for that quarter among the unitholders and our general partner in the following manner:

*first*, 98% to all unitholders, pro rata, and 2% to our general partner, until each unitholder receives a total of \$0.244375 per unit for that quarter (the first target distribution );

*second*, 85% to all unitholders, pro rata, and 15% to our general partner, until each unitholder receives a total of \$0.265625 per unit for that quarter (the second target distribution );

*third*, 75% to all unitholders, pro rata, and 25% to our general partner, until each unitholder receives a total of \$0.318750 per unit for that quarter (the third target distribution ); and

*thereafter*, 50% to all unitholders, pro rata, and 50% to our general partner.

**Table of Contents****Percentage Allocations of Available Cash from Operating Surplus**

The following table illustrates the percentage allocations of available cash from operating surplus between the unitholders and our general partner based on the specified target distribution levels. The amounts set forth under Marginal percentage interest in distributions are the percentage interests of our general partner and the unitholders in any available cash from operating surplus we distribute up to and including the corresponding amount in the column Total quarterly distribution per unit target amount. The percentage interests shown for our unitholders and our general partner for the minimum quarterly distribution are also applicable to quarterly distribution amounts that are less than the minimum quarterly distribution. The percentage interests set forth below for our general partner include its 2% general partner interest and assume that our general partner has contributed any additional capital necessary to maintain its 2% general partner interest, our general partner has not transferred its incentive distribution rights and that there are no arrearages on common units.

	<b>Total quarterly distribution per unit target amount</b>	<b>Unitholders</b>	<b>Marginal percentage interest in distributions General Partner</b>
Minimum Quarterly Distribution	\$0.2125	98%	2%
First Target Distribution	above \$0.2125 up to \$0.244375	98%	2%
Second Target Distribution	above \$0.244375 up to \$0.265625	85%	15%
Third Target Distribution	above \$0.265625 up to \$0.318750	75%	25%
Thereafter	above \$0.318750	50%	50%

**General Partner's Right to Reset Incentive Distribution Levels**

Our general partner, as the initial holder of our incentive distribution rights, has the right under our partnership agreement, subject to certain conditions, to elect to relinquish the right to receive incentive distribution payments based on the initial target distribution levels and to reset, at higher levels, the minimum quarterly distribution amount and target distribution levels upon which the incentive distribution payments to our general partner would be set. If our general partner transfers all or a portion of the incentive distribution rights in the future, then the holder or holders of a majority of our incentive distribution rights will be entitled to exercise this right. The following discussion assumes that our general partner holds all of the incentive distribution rights at the time that a reset election is made. Our general partner's right to reset the minimum quarterly distribution amount and the target distribution levels upon which the incentive distributions payable to our general partner are based may be exercised, without approval of our unitholders or the conflicts committee, at any time when there are no subordinated units outstanding, we have made cash distributions to the holders of the incentive distribution rights at the highest level of incentive distributions for each of the four consecutive fiscal quarters immediately preceding such time and the amount of each such distribution did not exceed adjusted operating surplus for such quarter. If our general partner and its affiliates are not the holders of a majority of the incentive distribution rights at the time an election is made to reset the minimum quarterly distribution amount and the target distribution levels, then the proposed reset will be subject to the prior written concurrence of the general partner that the conditions described above have been satisfied. The reset minimum quarterly distribution amount and target distribution levels will be higher than the minimum quarterly distribution amount and the target distribution levels prior to the reset such that the holder of the incentive distribution rights will not receive any incentive distributions under the reset target distribution levels until cash distributions per unit following this event increase as described below. We anticipate that our general partner would exercise this reset right

in order to facilitate acquisitions or internal growth projects that would otherwise not be sufficiently accretive to cash distributions per common unit, taking into account the existing levels of incentive distribution payments being made to our general partner.

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In connection with the resetting of the minimum quarterly distribution amount and the target distribution levels and the corresponding relinquishment by our general partner of incentive distribution payments based on the target distributions prior to the reset, our general partner will be entitled to receive a number of newly issued common units based on a predetermined formula described below that takes into account the cash parity value of the average cash distributions related to the incentive distribution rights received by our general partner for the two quarters immediately preceding the reset event as compared to the average cash distributions per common unit during that two-quarter period. In addition, our general partner will be issued the number of general partner units necessary to maintain our general partner's interest in us immediately prior to the reset election.

The number of common units that our general partner (or the then-holder of the incentive distribution rights, if other than our general partner) would be entitled to receive from us in connection with a resetting of the minimum quarterly distribution amount and the target distribution levels then in effect would be equal to the quotient determined by dividing (x) the average aggregate amount of cash distributions received by our general partner in respect of its incentive distribution rights during the two consecutive fiscal quarters ended immediately prior to the date of such reset election by (y) the average of the aggregate amount of cash distributed per common unit during each of these two quarters.

Following a reset election, the minimum quarterly distribution amount will be reset to an amount equal to the average cash distribution amount per common unit for the two fiscal quarters immediately preceding the reset election (which amount we refer to as the reset minimum quarterly distribution ) and the target distribution levels will be reset to be correspondingly higher such that we would distribute all of our available cash from operating surplus for each quarter thereafter as follows:

*first*, 98% to all unitholders, pro rata, and 2% to our general partner, until each unitholder receives an amount equal to 115% of the reset minimum quarterly distribution for that quarter;

*second*, 85% to all unitholders, pro rata, and 15% to our general partner, until each unitholder receives an amount per unit equal to 125% of the reset minimum quarterly distribution for the quarter;

*third*, 75% to all unitholders, pro rata, and 25% to our general partner, until each unitholder receives an amount per unit equal to 150% of the reset minimum quarterly distribution for the quarter; and

*thereafter*, 50% to all unitholders, pro rata, and 50% to our general partner.

Our general partner will be entitled to cause the minimum quarterly distribution amount and the target distribution levels to be reset on more than one occasion, provided that it may not make a reset election except at a time when it has received incentive distributions for the immediately preceding four consecutive fiscal quarters based on the highest level of incentive distributions that it is entitled to receive under our partnership agreement.

**Distributions from Capital Surplus*****How distributions from capital surplus will be made***

Assuming our general partner maintains its 2% general partner interest and we do not issue additional classes of equity securities, we will make distributions of available cash from capital surplus, if any, in the following manner:

*first*, 98% to all unitholders, pro rata, and 2% to our general partner, until we distribute for each common unit that was issued in our initial public offering, an amount of available cash from capital surplus equal to the initial public offering price;

*second*, 98% to all unitholders, pro rata, and 2% to our general partner, until we distribute for each common unit, an amount of available cash from capital surplus equal to any unpaid arrearages in payment of the minimum quarterly distribution on the outstanding common units; and

*thereafter*, as if they were from operating surplus.

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***Effect of a distribution from capital surplus***

Our partnership agreement treats a distribution of capital surplus as the repayment of the initial unit price from our initial public offering, which is a return of capital. The initial public offering price less any distributions of capital surplus per unit is referred to as the unrecovered initial unit price. Each time a distribution of capital surplus is made, the minimum quarterly distribution and the target distribution levels will be reduced in the same proportion as the corresponding reduction in the unrecovered initial unit price. Because distributions of capital surplus will reduce the minimum quarterly distribution after any of these distributions are made, the effects of distributions of capital surplus may make it easier for our general partner to receive incentive distributions. However, any distribution of capital surplus before the unrecovered initial unit price is reduced to zero cannot be applied to the payment of the minimum quarterly distribution or any arrearages.

Once we distribute capital surplus on a unit issued in our initial public offering in an amount equal to the initial unit price, we will reduce the minimum quarterly distribution and the target distribution levels to zero. Then, after distributing an amount of capital surplus for each common unit equal to any unpaid arrearages of the minimum quarterly distributions on outstanding common units, we will then make all future distributions from operating surplus, with 50% being paid to the unitholders, pro rata, and 2% to our general partner and 48% to the holder of our incentive distribution rights.

**Adjustment to the Minimum Quarterly Distribution and Target Distribution Levels**

In addition to adjusting the minimum quarterly distribution and target distribution levels to reflect a distribution of capital surplus, if we combine our units into fewer units or subdivide our units into a greater number of units, we will proportionately adjust:

the minimum quarterly distribution;

target distribution levels;

the unrecovered initial unit price;

the number of general partner units comprising the general partner interest; and

the arrearages per common unit in payment of the minimum quarterly distribution on the common units. For example, if a two-for-one split of the common units should occur, the minimum quarterly distribution, the target distribution levels and the unrecovered initial unit price would each be reduced to 50% of its initial level, and each general partner unit would be split into two units. We will not make any adjustment by reason of the issuance of additional units for cash or property (including additional common units issued under any compensation or benefit plans).

In addition, if legislation is enacted or if the official interpretation of existing law is modified by a governmental authority, so that we become taxable as a corporation or otherwise subject to taxation as an entity for federal, state or



local income tax purposes, our partnership agreement specifies that the minimum quarterly distribution and the target distribution levels for each quarter may be reduced by multiplying each distribution level by a fraction, the numerator of which is available cash for that quarter (reduced by the amount of the estimated tax liability for such quarter payable by reason of such legislation or interpretation) and the denominator of which is the sum of available cash for that quarter (reduced by the amount of the estimated tax liability for such quarter payable by reason of such legislation or interpretation) plus our general partner's estimate of our aggregate liability for the quarter for such income taxes payable by reason of such legislation or interpretation. To the extent that the actual tax liability differs from the estimated tax liability for any quarter, the difference may be accounted for in subsequent quarters.

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**Distributions of Cash Upon Liquidation**

***General***

If we dissolve in accordance with our partnership agreement, we will sell or otherwise dispose of our assets in a process called liquidation. We will first apply the proceeds of liquidation to the payment of our creditors. We will distribute any remaining proceeds to the unitholders and our general partner, in accordance with their capital account balances, as adjusted to reflect any gain or loss upon the sale or other disposition of our assets in liquidation.

***Manner of adjustments for gain***

The manner of the adjustment for gain is set forth in our partnership agreement. We will allocate any gain to our partners in the following manner:

*first*, to our general partner to the extent of any negative balance in its capital account;

*second*, 98% to the common unitholders, pro rata, and 2% to our general partner, until the capital account for each common unit is equal to the sum of:

- (1) the unrecovered initial unit price; and
- (2) the amount of the minimum quarterly distribution for the quarter during which our liquidation occurs.

*third*, 98% to all unitholders, pro rata, and 2% to our general partner, until we allocate under this paragraph an amount per unit equal to:

- (1) the sum of the excess of the first target distribution per unit over the minimum quarterly distribution per unit for each quarter of our existence;