HOLLY ENERGY PARTNERS LP
Form 10-Q
May 05, 2008

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

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

For the quarterly period ended March 31, 2008

OR

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

For the transition period from __________ to __________.

Commission File Number: 1-32225

HOLLY ENERGY PARTNERS, L.P.

(Exact name of registrant as specified in its charter)

Delaware	20-0833098
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

100 Crescent Court, Suite 1600
Dallas, Texas 75201-6915
(Address of principal executive offices)
(214) 871-3555
(Registrant s telephone number, including area code)
None
(Former name, former address and former fiscal year, if changed since last report)

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 þ No o

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

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

Indicate by check mark whether the registrant is a shell company (as defined by Rule 12b-2 of the Exchange Act).

Yes o No þ

The number of the registrant s outstanding common units at April 30, 2008 was 8,390,000.

HOLLY ENERGY PARTNERS, L.P.

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PART I. FINANCIAL INFORMATION

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. These statements are based on management s beliefs and assumptions 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 believe that the expectations reflected in these forward-looking statements are reasonable, we cannot assure you that our expectations will prove correct. Therefore, actual outcomes and results could differ materially from what is expressed, implied or forecast in these statements. Any differences could be caused by a number of factors, including, but 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 in our terminals;
- The economic viability of Holly Corporation, Alon USA, Inc. and our other customers;
- The demand for refined petroleum products and crude oil in markets we serve;
- Our ability to successfully purchase and integrate additional operations in the future;
- Our ability to complete previously announced pending or contemplated acquisitions;
- The availability and cost of our 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, operations 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, in conjunction with the forward-looking statements included in this Form 10-Q that are referred to above. When considering forward-looking statements, you should keep in mind the risk factors and other cautionary statements set forth in our Annual Report on Form 10-K for the year ended December 31, 2007 in Risk Factors, and in this Form 10-Q in Management s Discussion and Analysis of Financial Condition and Results of Operations . 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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Item 1. Financial Statements

Holly Energy Partners, L.P.
Consolidated Balance Sheets

	March 31, 2008 (Unaudited)	December 31, 2007
	(In thousands, except unit data)	
ASSETS		
Current assets:		
Cash and cash equivalents	$ 8,237	$ 10,321
Accounts receivable:		
Trade	5,184	6,611
Affiliates	7,773	5,700
	12,957	12,311
Prepaid and other current assets	342	546
Total current assets	21,536	23,178
Properties and equipment, net	274,187	158,600
Transportation agreements, net	125,374	54,273
Other assets	6,209	2,853
Total assets	$ 427,306	$ 238,904
LIABILITIES AND PARTNERS EQUITY		
Current liabilities:		
Accounts payable	$ 4,773	$ 3,011
Accounts payable affiliates	5,068	6,021
Accrued interest	1,027	2,996
Deferred revenue	5,551	3,700
Accrued property taxes	626	1,177
Other current liabilities	651	827
Short-term borrowings under credit agreement	10,000	
Total current liabilities	27,696	17,732
Commitments and contingencies		
Long-term debt	356,330	181,435
Other long-term liabilities	4,695	1,181
Minority interest	11,145	10,740
Partners equity (deficit):		
Common unitholders (8,390,000 and 8,170,000 units issued and outstanding at March 31, 2008 and December 31, 2007, respectively)	179,034	172,807

Subordinated unitholders (7,000,000 units issued and outstanding)	(75,779)	(73,725)
Class B subordinated unitholders (937,500 units issued and outstanding)	22,697	22,973
General partner interest (2% interest)	(94,163)	(94,239)
Accumulated other comprehensive loss	(4,349)	
Total partners equity	27,440	27,816
Total liabilities and partners equity	$ 427,306	$ 238,904

See accompanying notes.

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Holly Energy Partners, L.P.
Consolidated Statements of Income
(Unaudited)

	Three Months Ended March 31, 2008	Three Months Ended March 31, 2007
	(In thousands, except per unit data)	
Revenues:		
Affiliates	$ 18,318	$ 13,790
Third parties	8,958	10,082
	27,276	23,872
Operating costs and expenses:		
Operations	9,727	7,733
Depreciation and amortization	4,313	4,071
General and administrative	1,286	1,272
	15,326	13,076
Operating income	11,950	10,796
Other income (expense):		
Interest income	93	185
Interest expense	(3,807)	(3,358)
Gain on sale of assets	36	297
Minority interest in Rio Grande Pipeline Company	(406)	(427)
	(4,084)	(3,303)
Income before income taxes	7,866	7,493
State income tax	(68)	(59)
Net income	7,798	7,434
Less general partner interest in net income	821	580
Limited partners interest in net income	$ 6,977	$ 6,854
Net income per limited partner unit - basic and diluted	$ 0.43	$ 0.43

Weighted average limited partners units outstanding	16,181	16,108

See accompanying notes.

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Holly Energy Partners, L.P.
Consolidated Statements of Cash Flows
(Unaudited)

	Three Months Ended March 31,	
	2008	**2007**
	(In thousands)	
Cash flows from operating activities		
Net income	$ 7,798	$ 7,434
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	4,313	4,071
Minority interest in Rio Grande Pipeline Company	405	427
Amortization of restricted and performance units	94	302
Gain on sale of assets	(36)	(297)
(Increase) decrease in current assets:		
Accounts receivable	1,427	1,768
Accounts receivable affiliates	(2,073)	1,652
Prepaid and other current assets	204	391
Increase (decrease) in current liabilities:		
Accounts payable	1,762	(1,664)
Accounts payable affiliates	(953)	
Accrued interest	(1,969)	(1,953)
Deferred revenue	1,851	906
Accrued property tax	(551)	(360)
Other current liabilities	(177)	(368)
Other, net	309	284
Net cash provided by operating activities	12,404	12,593
Cash flows from investing activities		
Additions to properties and equipment	(11,086)	(912)
Acquisition of crude pipelines and tankage assets	(171,000)	
Proceeds from sale of assets	36	325
Net cash used for investing activities	(182,050)	(587)
Cash flows from financing activities		
Borrowings under credit agreement	181,000	
Proceeds from issuance of common units	104	
Distributions to partners	(12,623)	(11,538)
Cash contribution from general partner	186	
Purchase of units for restricted grants	(514)	(908)
Deferred financing costs	(591)	
Other		(15)
Net cash provided by (used for) financing activities	167,562	(12,461)

Cash and cash equivalents		
Decrease for period	(2,084)	(455)
Beginning of period	10,321	11,555
End of period	$ 8,237	$ 11,100

See accompanying notes.

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Holly Energy Partners, L.P.
Consolidated Statement of Partners Equity (Deficit) and Comprehensive Income
(Unaudited)

	Common Units	Subordinated Units	Class B Subordinated Units	General Partner Interest	Accumulated Other Comprehensive Loss	Total
			(In thousands)			
Balance December 31, 2007	$ 172,807	$ (73,725)	$ 22,973	$ (94,239)	$	$ 27,816
Net income	3,552	3,021	404	821		7,798
Change in fair value of cash flow hedge					(4,349)	(4,349)
Comprehensive income	3,552	3,021	404	821	(4,349)	3,449
Distributions to partners	(5,938)	(5,075)	(680)	(931)		(12,624)
Issuance of common units	9,104					9,104
Cost of issuing common units	(71)					(71)
Capital contribution				186		186
Purchase of units for restricted grants	(514)					(514)
Amortization of restricted and performance units	94					94
Balance March 31, 2008	$ 179,034	$ (75,779)	$ 22,697	$ (94,163)	$ (4,349)	$ 27,440

See accompanying notes.

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, currently 46% owned by Holly Corporation and its subsidiaries (collectively Holly). HEP commenced operations July 13, 2004 upon the completion of its initial public offering. In this document, the words we , our , ours and us refer to HEP unless the context otherwise indicates.

We operate in one business segment the operation of petroleum product and crude gathering pipelines, tankage and terminal facilities.

One of Holly s wholly-owned subsidiaries owns a refinery in Artesia, New Mexico, which Holly operates in conjunction with crude, vacuum distillation and other facilities situated in Lovington, New Mexico (collectively, the Navajo Refinery). The Navajo Refinery produces high-value refined products such as gasoline, diesel fuel and jet fuel and serves markets in the southwestern United States and northern Mexico. We own and operate the two parallel intermediate feedstock pipelines (the Intermediate Pipelines), which connect the New Mexico refining facilities. Our refined product pipelines serve as part of the product distribution network that services the Navajo Refinery. Our terminal operations serving the Navajo Refinery include a truck rack at the Navajo Refinery and four integrated refined product terminals located in New Mexico, Texas and Arizona. On February 29, 2008, we acquired pipeline and tankage assets from Holly (the Crude Pipelines and Tankage Assets) that also service the Navajo Refinery. See Note 2 for a further description of these assets.

Another of Holly s wholly-owned subsidiaries owns a refinery located near Salt Lake City, Utah (the Woods Cross Refinery). Our operations serving the Woods Cross Refinery include a truck rack at the Woods Cross Refinery, a refined product terminal in Spokane, Washington and a 50% non-operating interest in product terminals in Boise and Burley, Idaho. See Note 2 for a description of the Crude Pipelines and Tankage Assets that also service the Woods Cross refinery.

We also own and operate refined products pipelines and terminals, located primarily in Texas, that service Alon USA, Inc. s refinery in Big Spring, Texas.

Additionally, we own a refined product terminal in Mountain Home, Idaho, and a 70% interest in Rio Grande Pipeline Company (Rio Grande), which provides transportation of liquid petroleum gases to northern Mexico.

The consolidated financial statements for the three months ended March 31, 2008 and 2007 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, that, 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 accounting principles generally accepted in the United States of America 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 Form 10-K for the year ended December 31, 2007. 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, 2008.

We have reclassified state income taxes for the three months ended March 31, 2007 to conform to our current presentation at March 31, 2008. State income taxes were previously classified as operations and general and administrative expenses in our consolidated statement of income for the three months ended March 31, 2007.

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Recent Accounting Pronouncements

Statement of Financial Accounting Standards (SFAS) No. 157 Fair Value Measurements

In September 2006, the Financial Accounting Standards Board (FASB) issued SFAS No. 157, Fair Value Measurements. This standard simplifies and codifies guidance on fair value measurements under generally accepted accounting principles. This standard defines fair value, establishes a framework for measuring fair value and prescribes expanded disclosures about fair value measurements. It also establishes a fair value hierarchy that categorizes inputs used in fair value measurements into three broad levels. Under this hierarchy, quoted prices in active markets for identical assets or liabilities are considered the most reliable evidence of fair value and are given the highest priority level (level 1). Unobservable inputs are considered the least reliable and are given the lowest priority level (level 3). We adopted this standard effective January 1, 2008.

We have interest rate swaps that we measure at fair value on a recurring basis using level 2 inputs. See Note 5 in the Notes to the Consolidated Financial Statements for additional information on these swaps.

SFAS No. 133 Implementation Issue No. E23 Issues Involving the Application of the Shortcut Method under Paragraph 68

In January 2008, the FASB posted SFAS No. 133 Implementation Issue No. E23, Issues Involving the Application of the Shortcut Method under Paragraph 68. This standard addresses issues pertaining to the application of the shortcut method in accounting for hedges when the settlement of a hedged item occurs subsequent to the interest rate swap trade date. It also addresses hedging relationships when the transaction price of an interest rate swap is zero. This standard is effective for hedging relationships designated on or after January 1, 2008 and requires the reassessment of preexisting hedges utilizing the shortcut method under this new guidance. We adopted this standard effective January 1, 2008. The adoption of this standard did not have a material impact on our financial condition, results of operations and cash flows.

Note 2: Acquisition

On February 29, 2008, we acquired the Crude Pipelines and Tankage Assets from Holly for $180.0 million that consist of crude oil trunk lines that deliver crude oil to Holly s Navajo Refinery in southeast New Mexico, gathering and connection pipelines located in west Texas and New Mexico, on-site crude tankage located within the Navajo and Woods Cross refinery complexes, a jet fuel products pipeline and leased terminal between Artesia and Roswell, New Mexico, and crude oil and product pipelines that support Holly s Woods Cross Refinery. The consideration paid for the Crude Pipelines and Tankage Assets consisted of $171.0 million in cash and 217,497 of our common units having a fair value of $9.0 million. We financed the $171.0 million cash portion of the consideration through borrowings under our senior secured revolving credit agreement expiring August 2011.

In connection with this transaction, we entered into a 15-year crude pipelines and tankage agreement with Holly (the Holly CPTA). Under this agreement, Holly agreed to transport and store volumes of crude oil on the crude pipelines and tankage facilities, respectively that, at the agreed rates, will initially result in minimum annual revenues to us of $25.3 million. The agreed upon tariffs on the crude pipelines will be adjusted each year at a rate equal to the percentage change in the producer price index (PPI) but will not decrease as a result of a decrease in the PPI. Additionally, Holly amended our omnibus agreement (the Omnibus Agreement) to provide $7.5 million of indemnification for environmental noncompliance and remediation liabilities associated with the Crude Pipelines and Tankage Assets that occurred or existed prior to our acquisition for a period of up to fifteen years.

The consideration paid for the Crude Pipeline and Tankage Assets was allocated to the individual assets acquired based on management s preliminary fair value estimates. In accounting for this acquisition, we recorded pipeline and terminal assets of $108.0 and an intangible asset of $72.0 million, representing the allocated value of the Holly CPTA. This intangible asset is included in Transportation agreements, net in our consolidated balance sheets.

In accordance with the provisions of FASB Interpretation (FIN) No. 46, Holly recognizes us as a variable interest entity (VIE). Under this standard, our purchase of Holly s Crude Pipelines and Tankage Assets qualifies as a reconsideration event whereby Holly reassessed their beneficial interest in us. Following our acquisition of these assets, Holly determined that their beneficial interest in us now exceeds 50%. Accordingly, Holly reconsolidated us effective March 1, 2008.

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Note 3: Properties and Equipment

	March 31, 2008	December 31, 2007
	(In thousands)	
Pipelines and terminals	$ 305,088	$ 196,800
Land and right of way	23,977	22,825
Other	6,394	5,706
Construction in progress	18,061	9,103
	353,520	234,434
Less accumulated depreciation	79,333	75,834
	$ 274,187	$ 158,600

During the three months ended March 31, 2008 we capitalized $0.2 million in interest related to major construction projects. We did not capitalize any interest during the three months ended March 31, 2007.

Note 4: Transportation Agreements

Our transportation recorded agreements consist of the following:

The transportation agreement with Alon USA, Inc (Alon) represents a portion of the total purchase price of assets purchased from Alon in 2005 that was allocated based on an estimated fair value derived under the income approach. This asset is being amortized over 30 years ending 2035, the 15-year initial term of the pipelines and terminals agreement with Alon plus the expected 15-year extension period.

The Holly crude pipelines and tankage agreement represents a portion of the total purchase price of the Crude Pipelines and Tankage Assets that was allocated based on management s preliminary estimate of its fair value. This asset is being amortized over 15 years ending 2023, the 15-year term of the Holly CPTA.

The carrying amounts of our transportation agreements are as follows:

	March 31, 2008	December 31, 2007
	(In thousands)	
Alon transportation agreement	$ 59,933	$ 59,933
Holly crude pipelines and tankage agreement	72,000	
	131,933	59,933
Less accumulated amortization	6,559	5,660
	$ 125,374	$ 54,273

Note 5: Debt

Credit Agreement

In February 2008, we amended our $100 million senior secured revolving credit agreement expiring in August 2011 to increase the size from $100 million to $300 million (the Credit Agreement), which we used to finance the $171.0 million cash portion of the consideration paid for the Crude Pipelines and Tankage Assets acquired from Holly. Union Bank of California, N.A. is one of the lenders and serves as administrative agent under this agreement. As of March 31, 2008 and December 31, 2007, we had $181.0 million and zero, respectively, outstanding under the

Credit Agreement.

The Credit Agreement is available to fund capital expenditures, acquisitions, and working capital and for general partnership purposes. Advances under the Credit Agreement that are either designated for working capital or have been used as interim financing to fund capital expenditures are classified as

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short-term liabilities. Other advances under the Credit Agreement are classified as long-term liabilities. In addition, the Credit Agreement is available to fund letters of credit up to a $50.0 million sub-limit and to fund distributions to unitholders up to a $20.0 million sub-limit. During the three months ended March 31, 2008, we received advances totaling $10.0 million under the Credit Agreement that were used to fund capital expenditures.

We have the right to request an increase in the maximum amount of the Credit Agreement, up to $370.0 million. Such request will become effective if (a) certain conditions specified in the Credit Agreement are met and (b) existing lenders under the Credit Agreement or other financial institutions reasonably acceptable to the administrative agent commit to lend such increased amounts under the agreement.

Our obligations under the Credit Agreement are secured by substantially all of our assets. Indebtedness under the Credit Agreement is recourse to HEP Logistics Holdings, L.P., our general partner, and guaranteed by our wholly-owned subsidiaries.

We may prepay all loans at any time without penalty, except for payment of certain breakage and related costs. We are required to reduce all working capital borrowings under the Credit Agreement to zero for a period of at least 15 consecutive days once each twelve-month period prior to the maturity date of the agreement.

Indebtedness under the Credit Agreement bears interest, at our option, at either (a) the reference rate as announced by the administrative agent plus an applicable margin (ranging from 0.25% to 1.50%) or (b) at a rate equal to the London Interbank Offered Rate (LIBOR) plus an applicable margin (ranging from 1.00% to 2.50%). In each case, the applicable margin is based upon the ratio of our funded debt (as defined in the agreement) to EBITDA (earnings before interest, taxes, depreciation and amortization, as defined in the Credit Agreement). We incur a commitment fee on the unused portion of the Credit Agreement at a rate ranging from 0.20% to 0.50% based upon the ratio of our funded debt to EBITDA for the four most recently completed fiscal quarters. At March 31, 2008, we are subject to the 0.25% rate on the $119.0 million of the unused commitment on the Credit Agreement. The agreement matures in August 2011. At that time, the agreement will terminate and all outstanding amounts thereunder will be due and payable.

The Credit Agreement imposes certain requirements, including: a prohibition against distribution to unitholders if, before or after the distribution, a potential default or an event of default as defined in the agreement would occur; limitations on our ability to incur debt, make loans, acquire other companies, change the nature of our business, enter a merger or consolidation, or sell assets; and covenants that require maintenance of a specified EBITDA to interest expense ratio and debt to EBITDA ratio. If an event of default exists under the agreement, the lenders will be able to accelerate the maturity of the debt and exercise other rights and remedies.

Senior Notes Due 2015

Our senior notes maturing March 1, 2015 are registered with the SEC and bear interest at 6.25% (the Senior Notes). The Senior Notes are unsecured and impose certain restrictive covenants, including limitations on our ability to incur additional indebtedness, make investments, sell assets, incur certain liens, pay distributions, enter into transactions with affiliates, and enter into mergers. At any time when the Senior Notes are rated investment grade by both Moody s and Standard & Poor s and no default or event of default exists, we will not be subject to many of the foregoing covenants. Additionally, we have certain redemption rights under the Senior Notes.

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The carrying amounts of our long-term debt are as follows:

	March 31, 2008	December 31, 2007
	(In thousands)	
Credit Agreement	$ 181,000	$
Senior Notes		
Principal	185,000	185,000
Unamortized discount	(2,629)	(2,724)
Fair value hedge interest rate swap	2,959	(841)
	185,330	181,435
Total Debt	366,330	181,435
Less short-term borrowing under credit agreement	10,000	
Total long-term debt	$ 356,330	$ 181,435

Interest Rate Risk Management

As of March 31, 2008, we have two interest rate swap contracts.

We entered into an interest rate swap to hedge our exposure to the cash flow risk caused by the effects of LIBOR changes on the $171.0 million Credit Agreement advance that we used to finance our purchase of the Crude Pipelines and Tankage Assets from Holly. This interest rate swap effectively converts our $171.0 million LIBOR based debt to fixed rate debt having an interest rate of 3.74% plus an applicable margin, currently 1.50%, that results in a March 31, 2008 effective interest rate of 5.24%.

Under the provisions of SFAS No. 133, we have designated this interest rate swap as a cash flow hedge. Based on our assessment of effectiveness using the change in variable cash flows method, we have determined that this interest rate swap is effective in offsetting the variability in interest payments on our $171.0 million variable rate debt resulting from changes in LIBOR. Under hedge accounting, we adjust our cash flow hedge on a quarterly basis to its fair value with a corresponding offset to accumulated other comprehensive income. Also on a quarterly basis, we measure hedge effectiveness by comparing the present value of the cumulative change in the expected future interest payments on the variable leg of our swap against the expected future interest payments on our $171.0 million variable rate debt. Any ineffectiveness is reclassified from accumulated other comprehensive income to interest expense. As of March 31, 2008, we had no ineffectiveness on our cash flow hedge.

We also have an interest rate swap contract that effectively converts interest expense associated with $60.0 million of our 6.25% Senior Notes from a fixed to a variable rate. Under this swap contract, interest on the $60.0 million notional amount is computed using the three-month LIBOR plus an applicable margin of 1.1575%, which equaled an effective interest rate of 4.23% at March 31, 2008. The maturity of the swap contract is March 1, 2015, matching the maturity of the Senior Notes.

This interest rate swap has been designated as a fair value hedge and meets the requirements to assume no ineffectiveness under the provisions of SFAS No. 133. Accordingly, we use the shortcut method of accounting as prescribed under SFAS No. 133. Under this method, we adjust the carrying value of the swap to its fair value on a quarterly basis, with an offsetting entry to our Senior Notes, effectively adjusting the carrying value of $60.0 million of principal on the Senior notes to its fair value.

We record interest expense equal to the variable rate payments under the swaps. Receipts under the swap agreements are recorded as a reduction of interest expense.