

HOLLY ENERGY PARTNERS LP
Form 10-Q
May 04, 2016

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2016

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

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.) |

| | |
|--|------------|
| 2828 N. Harwood, Suite 1300 | 75201 |
| Dallas, Texas | |
| (Address of principal executive offices) | (Zip code) |
| (214) 871-3555 | |
| (Registrant's telephone number, including area code) | |

(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 ☒ 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 April 29, 2016 was 58,657,048.

Table of Contentsril 19,

HOLLY ENERGY PARTNERS, L.P.
INDEX

| | |
|--|-----------|
| <u>FORWARD-LOOKING STATEMENTS</u> | <u>3</u> |
| <u>PART I. FINANCIAL INFORMATION</u> | <u>4</u> |
| Item 1. <u>Financial Statements (Unaudited)</u> | <u>4</u> |
| <u>Consolidated Balance Sheets</u> | <u>4</u> |
| <u>Consolidated Statements of Income</u> | <u>5</u> |
| <u>Consolidated Statements of Comprehensive Income</u> | <u>6</u> |
| <u>Consolidated Statements of Cash Flows</u> | <u>7</u> |
| <u>Consolidated Statements of Partners' Equity</u> | <u>8</u> |
| <u>Notes to Consolidated Financial Statements</u> | <u>9</u> |
| Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u> | <u>26</u> |
| Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u> | <u>36</u> |
| Item 4. <u>Controls and Procedures</u> | <u>36</u> |
| <u>PART II. OTHER INFORMATION</u> | <u>37</u> |
| Item 1. <u>Legal Proceedings</u> | <u>37</u> |
| Item 1A. <u>Risk Factors</u> | <u>37</u> |
| Item 6. <u>Exhibits</u> | <u>37</u> |
| <u>SIGNATURES</u> | <u>38</u> |
| <u>Index to Exhibits</u> | <u>39</u> |

Table of Contentsril 19,

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, 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.

Table of Contentsril 19,

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

HOLLY ENERGY PARTNERS, L.P.
CONSOLIDATED BALANCE SHEETS
(Unaudited)
(in thousands, except unit data)

| | March 31, 2016 | December 31, 2015 ⁽¹⁾ |
|----------------------------------|-------------------|-------------------------------------|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$9,034 | \$15,013 |
| Accounts receivable: | | |
| Trade | 7,936 | 8,593 |
| Affiliates | 33,120 | 32,482 |
| | 41,056 | 41,075 |
| Prepaid and other current assets | 5,181 | 5,054 |
| Total current assets | 55,271 | 61,142 |
| Properties and equipment, net | 1,052,772 | 1,059,179 |
| Transportation agreements, net | 72,067 | 73,805 |
| Goodwill | 256,498 | 256,498 |
| Equity method investments | 124,134 | 79,438 |
| Other assets | 11,819 | 13,703 |
| Total assets | \$1,572,561 | \$1,543,765 |
| LIABILITIES AND EQUITY | | |
| Current liabilities: | | |
| Accounts payable: | | |
| Trade | \$12,305 | \$10,948 |
| Affiliates | 6,175 | 11,635 |
| | 18,480 | 22,583 |
| Accrued interest | 1,972 | 6,752 |
| Deferred revenue | 7,050 | 12,016 |
| Accrued property taxes | 4,107 | 3,764 |
| Other current liabilities | 2,945 | 3,809 |
| Total current liabilities | 34,554 | 48,924 |
| Long-term debt | 1,061,944 | 1,008,752 |
| Other long-term liabilities | 16,397 | 20,744 |
| Deferred revenue | 39,441 | 39,063 |
| Class B unit | 35,807 | 33,941 |
| Equity: | | |
| Partners' equity: | | |

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| | | |
|---|-------------|-------------|
| Common unitholders (58,657,048 units issued and outstanding at March 31, 2016 and December 31, 2015) | 425,669 | 428,019 |
| General partner interest (2% interest) | (137,228) | (130,297) |
| Accumulated other comprehensive income (loss) | (263) | 190 |
| Total partners' equity | 288,178 | 297,912 |
| Noncontrolling interest | 96,240 | 94,429 |
| Total equity | 384,418 | 392,341 |
| Total liabilities and equity | \$1,572,561 | \$1,543,765 |

(1) Retrospectively adjusted as described in Note 1.

See accompanying notes.

Table of Contentsril 19,

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

| | Three Months Ended March 31, | |
|---|---------------------------------|---------------------|
| | 2016 | 2015 ⁽¹⁾ |
| Revenues: | | |
| Affiliates | \$82,846 | \$72,255 |
| Third parties | 19,164 | 17,501 |
| | 102,010 | 89,756 |
| Operating costs and expenses: | | |
| Operations (exclusive of depreciation and amortization) | 26,922 | 28,065 |
| Depreciation and amortization | 16,551 | 14,798 |
| General and administrative | 3,091 | 3,290 |
| | 46,564 | 46,153 |
| Operating income | 55,446 | 43,603 |
| Other income (expense): | | |
| Equity in earnings of equity method investments | 2,765 | 734 |
| Interest expense | (10,535) | (8,768) |
| Interest income | 112 | — |
| Gain on sale of assets | — | 159 |
| Other expense | (8) | — |
| | (7,666) | (7,875) |
| Income before income taxes | 47,780 | 35,728 |
| State income tax expense | (95) | (101) |
| Net income | 47,685 | 35,627 |
| Allocation of net income attributable to noncontrolling interests | (4,927) | (4,027) |
| Net income attributable to Holly Energy Partners | 42,758 | 31,600 |
| General partner interest in net income, including incentive distributions | (11,886) | (9,607) |
| Limited partners' interest in net income | \$30,872 | \$21,993 |
| Limited partners' per unit interest in earnings—basic and diluted | \$0.52 | \$0.37 |
| Weighted average limited partners' units outstanding | 58,657 | 58,657 |

(1) Retrospectively adjusted as described in Note 1.

See accompanying notes.

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

| | Three Months Ended March 31, | |
|--|---------------------------------|---------------------|
| | 2016 | 2015 ⁽¹⁾ |
| Net income | \$47,685 | \$35,627 |
| Other comprehensive income: | | |
| Change in fair value of cash flow hedging instruments | (683) | (1,280) |
| Reclassification adjustment to net income on partial settlement of cash flow hedge | 230 | 531 |
| Other comprehensive income (loss) | (453) | (749) |
| Comprehensive income before noncontrolling interest | 47,232 | 34,878 |
| Allocation of comprehensive income to noncontrolling interests | (4,927) | (4,027) |
| Comprehensive income attributable to Holly Energy Partners | \$42,305 | \$30,851 |

(1) Retrospectively adjusted as described in Note 1.

See accompanying notes.

Table of Contentsril 19,

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

| | Three Months Ended March 31, | |
|---|---------------------------------|---------------------|
| | 2016 | 2015 ⁽¹⁾ |
| Cash flows from operating activities | | |
| Net income | \$47,685 | \$35,627 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 16,551 | 14,798 |
| (Gain) loss on sale of assets | — | (159) |
| Amortization of deferred charges | 593 | 436 |
| Amortization of restricted and performance units | 651 | 896 |
| Distributions less than income from equity investments | (365) | — |
| (Increase) decrease in operating assets: | | |
| Accounts receivable—trade | 657 | (5,065) |
| Accounts receivable—affiliates | (637) | 5,804 |
| Prepaid and other current assets | (128) | 39 |
| Increase (decrease) in operating liabilities: | | |
| Accounts payable—trade | (1,082) | 1,748 |
| Accounts payable—affiliates | (5,460) | 10,564 |
| Accrued interest | (4,780) | (4,811) |
| Deferred revenue | (4,588) | (3,355) |
| Accrued property taxes | 343 | 42 |
| Other current liabilities | (843) | 57 |
| Other, net | (295) | 4,171 |
| Net cash provided by operating activities | 48,302 | 60,792 |
| Cash flows from investing activities | | |
| Additions to properties and equipment | (17,873) | (24,227) |
| Purchase of El Dorado crude tanks | — | (27,500) |
| Proceeds from sale of assets and other | 12 | 218 |
| Distributions in excess of equity in earnings of equity investments | 99 | 16 |
| Net cash used for investing activities | (17,762) | (51,493) |
| Cash flows from financing activities | | |
| Borrowings under credit agreement | 522,000 | 153,500 |
| Repayments of credit agreement borrowings | (469,000) | (130,500) |
| Contributions from HFC for El Dorado Operating acquisition | — | 12,563 |
| Distributions to HEP unitholders | (44,960) | (40,865) |
| Distributions to noncontrolling interest | (1,250) | (1,250) |
| Distribution to HFC for Tulsa Tank acquisition | (39,500) | — |
| Contributions from HFC for Tulsa Tank expenditures | 99 | 472 |
| Purchase of units for incentive grants | (784) | (247) |
| Deferred financing costs | (2,964) | — |
| Other | (160) | — |
| Net cash used by financing activities | (36,519) | (6,327) |

| | | |
|------------------------------------|----------|---------|
| Cash and cash equivalents | | |
| Increase (decrease) for the period | (5,979) | 2,972 |
| Beginning of period | 15,013 | 2,830 |
| End of period | \$9,034 | \$5,802 |

(1) Retrospectively adjusted as described in Note 1.

See accompanying notes.

- 7 -

Table of Contentsril 19,

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

| | Common Units | General Partner Interest | Accumulated Other Comprehensive Loss | Noncontrolling Interest | Total Equity |
|---|-----------------|--------------------------------|---|----------------------------|-----------------|
| Balance December 31, 2015 ⁽¹⁾ | \$428,019 | \$(130,297) | \$ 190 | \$ 94,429 | \$392,341 |
| Contribution from HFC for Osage transaction | — | 32,455 | — | — | 32,455 |
| Distribution to HFC for Tulsa Tank acquisition | — | (39,500) | — | — | (39,500) |
| Contribution from HFC for Tulsa Tank expenditures | — | 99 | — | — | 99 |
| Distributions to HEP unitholders | (33,126) | (11,834) | — | — | (44,960) |
| Distributions to noncontrolling interest | — | — | — | (1,250) | (1,250) |
| Purchase of units for incentive grants | (784) | — | — | — | (784) |
| Amortization of restricted and performance units | 651 | — | — | — | 651 |
| Class B unit accretion | (1,829) | (37) | — | — | (1,866) |
| Net income | 32,738 | 11,886 | — | 3,061 | 47,685 |
| Other comprehensive loss | — | — | (453) | — | (453) |
| Balance March 31, 2016 | \$425,669 | \$(137,228) | \$ (263) | \$ 96,240 | \$384,418 |

(1) Retrospectively adjusted as described in Note 1.

See accompanying notes.

Table of Contentsril 19,

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, loading rack facilities and refinery processing units.

We own and operate petroleum product and crude oil pipelines, terminals, tankage and loading rack facilities and refinery processing units 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, a 50% interest in Frontier Pipeline Company, a 50% interest in Osage Pipe Line Company, LLC (“Osage”), and a 25% interest in SLC Pipeline LLC.

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, providing other services at our storage tanks and terminals and by charging fees for processing hydrocarbon feedstocks through our refinery processing units. We do not take ownership of products that we transport, terminal, store or process, 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, 2015. 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, 2016.

Acquisitions

Tulsa Tanks

On March 31, 2016, we acquired crude oil tanks located at HFC’s Tulsa refinery from an affiliate of Plains All American Pipeline, L.P. (“Plains”) for \$39.5 million. Previously in 2009, HFC sold these tanks to Plains and leased them back, and due to HFC’s continuing interest in the tanks, HFC accounted for the transaction as a financing arrangement. Accordingly, the tanks remained on HFC’s balance sheet and were depreciated for accounting purposes.

As we are a consolidated variable interest entity of HFC, this transaction was recorded as a transfer between entities under common control and reflects HFC’s carrying basis in the net assets acquired. We have retrospectively adjusted our financial position and operating results as if these crude oil tanks were owned for all periods while we were under common control of HFC. The 2015 consolidated income statement was adjusted to reflect a \$0.2 million increase in operating costs and expenses for the three months ended March 31, 2015, the consolidated balance sheet was adjusted

to reflect increases of \$9.3 million in net properties and equipment, \$0.1 million in other long-term liabilities and \$9.2 million in general partner interest at March 31, 2015. The consolidated statement of cash flows for the three months ended March 31, 2015, reflects these changes in cash flows from investing and financing activities.

In connection with this transaction, we expect to enter into a 10-year throughput agreement containing minimum quarterly throughput commitments from HFC that are expected to provide minimum annualized revenues of \$6.1 million.

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

Osage

On February 22, 2016, HFC obtained a 50% membership interest in Osage in a non-monetary exchange for a 20-year terminalling services agreement, whereby a subsidiary of Magellan Midstream Partners ("Magellan") will provide terminalling services for all HFC products originating in Artesia, New Mexico requiring terminalling in or through El Paso, Texas. Osage is the owner of the Osage Pipeline, a 135-mile pipeline that transports crude oil from Cushing, Oklahoma to HFC's El Dorado Refinery in Kansas and also connects to the Jayhawk pipeline serving the CHS Inc. refinery in McPherson, Kansas. The Osage Pipeline is the primary pipeline supplying HFC's El Dorado refinery with crude oil.

Concurrent with this transaction, we entered into a non-monetary exchange with HFC, whereby we received HFC's interest in Osage in exchange for our El Paso terminal. Under this exchange, we agreed to build two connections on our south products pipeline system that will permit HFC access to Magellan's El Paso terminal. Effective upon the closing of this exchange, we are the named operator of the Osage Pipeline and are working to transition into that role. Since we are a consolidated variable interest entity of HFC, this transaction was recorded as a transfer between entities under common control and reflects HFC's carrying basis of its 50% membership interest in Osage of \$44.0 million offset by our net carrying basis in the El Paso terminal of \$12.0 million with the difference treated as a contribution from HFC. The carrying value of our 50% membership interest in Osage of \$44.0 million exceeds the amount of the underlying equity in net assets recorded by Osage by \$33.0 million.

El Dorado Operating

On November 1, 2015, we acquired from HollyFrontier 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.

As we are a consolidated variable interest entity of HFC, this transaction was recorded as a transfer between entities under common control and reflects HFC's carrying basis in El Dorado Operating's assets and liabilities. We have retrospectively adjusted 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. The consolidated statement of cash flows for the three months ending March 31, 2015, reflects a \$12.6 million recast between investing activities and financing activities.

New Accounting Pronouncements

Revenue Recognition

In May 2014, an accounting standard update was issued requiring revenue to be recognized when promised goods or services are transferred to customers in an amount that reflects the expected consideration for these goods or services. This standard has an effective date of January 1, 2018. We are evaluating the impact of this standard.

Consolidation

In February 2015, the FASB issued a standard that modifies existing consolidation guidance for reporting organizations that are required to evaluate whether they should consolidate certain legal entities. We adopted the new standard effective January 1, 2016. This standard had no impact on the entities we consolidate.

Financial Assets and Liabilities

In January 2016, an accounting standard update was issued requiring changes in the accounting and disclosures for financial instruments. This standard will become effective beginning with our 2018 reporting year. We are evaluating the impact of this standard.

Leases

In February 2016, an accounting standard update was issued requiring leases to be measured and recognized as a lease liability, with a corresponding right-of-use asset on the balance sheet. This standard has an effective date of January 1, 2019, and we are evaluating the impact of this standard.

Earnings Per Unit

In April 2015, an accounting standard update was issued requiring changes to the allocation of the earnings or losses of a transferred business for periods before the date of a dropdown of net assets accounted for as a common control transaction entirely to the general partner for purposes of calculating historical earnings per unit. We have adopted this standard as of January 1, 2016, as

- 10 -

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

required. In connection with the dropdown of assets from HFC's Tulsa refinery on March 31, 2016, we reduced net income by \$0.2 million for the three months ending March 31, 2015. This reduction had no impact on the historical earnings per unit.

Note 2: Financial Instruments

Our financial instruments consist of cash and cash equivalents, accounts receivable, accounts payable, debt and interest rate swaps. The carrying amounts of cash and cash equivalents, accounts receivable and accounts payable approximate fair value due to the short-term maturity of these instruments. Debt consists of outstanding principal under our revolving credit agreement (which approximates fair value as interest rates are reset frequently at current interest rates) and our fixed interest rate senior notes.

Fair value measurements are derived using inputs (assumptions that market participants would use in pricing an asset or liability) including assumptions about risk. GAAP categorizes inputs used in fair value measurements into three broad levels as follows:

• Level 1) Quoted prices in active markets for identical assets or liabilities.

• Level 2) Observable inputs other than quoted prices included in Level 1, such as quoted prices for similar assets and liabilities in active markets, similar assets and liabilities in markets that are not active or can be corroborated by observable market data.

• Level 3) Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. This includes valuation techniques that involve significant unobservable inputs.

The carrying amounts and estimated fair values of our senior notes and interest rate swaps were as follows:

| | | March 31, 2016 | | December 31, 2015 | |
|----------------------|------------------------|----------------|------------|-------------------|------------|
| Financial Instrument | Fair Value Input Level | Carrying Value | Fair Value | Carrying Value | Fair Value |
| (In thousands) | | | | | |
| Assets: | | | | | |
| Interest rate swaps | Level 2 | \$— | \$— | \$304 | \$304 |
| Liabilities: | | | | | |
| 6.5% Senior notes | Level 2 | \$296,944 | \$295,500 | \$296,752 | \$295,500 |
| Interest rate swaps | Level 2 | 263 | 263 | 114 | 114 |
| | | \$297,207 | \$295,763 | \$296,866 | \$295,614 |

Level 2 Financial Instruments

Our senior notes and interest rate swaps are measured at fair value using Level 2 inputs. The fair value of the senior notes is based on market values provided by a third-party bank, which were derived using market quotes for similar type debt instruments. The fair value of our interest rate swaps is based on the net present value of expected future cash flows related to both variable and fixed-rate legs of the swap agreement. This measurement is computed using the forward London Interbank Offered Rate ("LIBOR") yield curve, a market-based observable input.

See Note 6 for additional information on these instruments.

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

Note 3: Properties and Equipment

The carrying amounts of our properties and equipment are as follows:

| | March 31, 2016 | December 31, 2015 ⁽¹⁾ |
|----------------------------------|-------------------|-------------------------------------|
| | (In thousands) | |
| Pipelines, terminals and tankage | \$1,200,516 | \$1,231,597 |
| Land and right of way | 65,274 | 66,215 |
| Refinery assets | 64,371 | 63,336 |
| Construction in progress | 43,201 | 28,249 |
| Other | 23,573 | 22,200 |
| | 1,396,935 | 1,411,597 |
| Less accumulated depreciation | 344,163 | 352,418 |
| | \$1,052,772 | \$1,059,179 |

(1) Retrospectively adjusted as described in Note 1.

We capitalized \$0.1 million and \$0.3 million in interest attributable to construction projects during the three months ended March 31, 2016 and 2015, respectively.

Depreciation expense was \$14.7 million and \$12.9 million for the three months ended March 31, 2016 and 2015, respectively.

Note 4: Transportation Agreements

Our transportation agreements represent a portion of the total purchase price of certain assets acquired from Alon in 2005 and from HFC in 2008. The Alon agreement is being amortized over 30 years ending 2035 (the initial 15-year term of the agreement plus an expected 15-year extension period), and the HFC agreement is being amortized over 15 years ending 2023 (the term of the HFC agreement).

The carrying amounts of our transportation agreements are as follows:

| | March 31, 2016 | December 31, 2015 |
|-------------------------------|-------------------|-------------------------|
| | (In thousands) | |
| Alon transportation agreement | \$59,933 | \$ 59,933 |
| HFC transportation agreement | 74,231 | 74,231 |
| Other | 50 | 50 |
| | 134,214 | 134,214 |
| Less accumulated amortization | 62,147 | 60,409 |
| | \$72,067 | \$ 73,805 |

We have additional transportation agreements with HFC resulting from historical transactions consisting of pipeline, terminal and tankage assets contributed to us or acquired from HFC. These transactions occurred while we were a

consolidated variable interest entity of HFC; therefore, our basis in these agreements is zero and does not reflect a step-up in basis to fair value.

Note 5: Employees, Retirement and Incentive Plans

Direct support for our operations is provided by Holly Logistic Services, L.L.C. (“HLS”), an HFC subsidiary, which utilizes personnel employed by HFC who are dedicated to performing services for us. Their costs, including salaries, bonuses, payroll taxes, benefits and other direct costs, are charged to us monthly in accordance with an omnibus agreement that we have with HFC. These employees participate in the retirement and benefit plans of HFC. Our share of retirement and benefit plan costs was \$1.6 million and \$1.4 million for the three months ended March 31, 2016 and 2015, respectively.

Under HLS’s secondment agreement with HFC (the “Secondment Agreement”), certain employees of HFC are seconded to HLS to provide operational and maintenance services for certain of our processing, refining, pipeline and tankage assets at the El Dorado,

- 12 -

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

Cheyenne and Tulsa refineries, and HLS reimburses HFC for its prorated portion of the wages, benefits, and other costs related to these employees.

We have a Long-Term Incentive Plan for employees and non-employee directors who perform services for us. The Long-Term Incentive Plan consists of four components: restricted or phantom units, performance units, unit options and unit appreciation rights.

As of March 31, 2016, we have two types of incentive-based awards outstanding, which are described below. The compensation cost charged against income was \$0.7 million and \$0.8 million for the three months ended March 31, 2016 and 2015, respectively. We currently purchase units in the open market instead of issuing new units for settlement of all unit awards under our Long-Term Incentive Plan. As of March 31, 2016, 2,500,000 units were authorized to be granted under our Long-Term Incentive Plan, of which 1,480,449 have not yet been granted, assuming no forfeitures of the unvested units and full achievement of goals for the performance units already granted.

Restricted and Phantom Units

Under our Long-Term Incentive Plan, we grant restricted units to non-employee directors and selected employees who perform services for us, with most awards vesting over a period of one to three years. Although full ownership of the units does not transfer to the recipients until the units vest, the recipients have distribution and voting rights on these units from the date of grant.

In addition, we previously granted phantom units to certain employees. All outstanding phantom units vested in 2015, and no phantom units are currently outstanding. Vested units were paid in common units. Full ownership of the units transferred to the recipients at vesting, and the recipients did not have voting or distribution rights on these units until they vested.

The fair value of each restricted unit award is measured at the market price as of the date of grant and is amortized on a straight-line basis over the requisite service period for each separately vesting portion of the award.

A summary of restricted unit activity and changes during the three months ended March 31, 2016, is presented below:

| Restricted Units | Units | Weighted Average Grant-Date Fair Value |
|--|---------|---|
| Outstanding at January 1, 2016 (nonvested) | 101,408 | \$ 33.63 |
| Granted | 10,725 | 24.48 |
| Outstanding at March 31, 2016 (nonvested) | 112,133 | \$ 32.76 |

As of March 31, 2016, there was \$2.2 million of total unrecognized compensation expense related to nonvested restricted unit grants, which is expected to be recognized over a weighted-average period of 1.3 years.

Performance Units

Under our Long-Term Incentive Plan, we grant performance units to selected executives who perform services for us. Performance units granted are payable in common units at the end of a three-year performance period based upon the growth in our distributable cash flow per common unit over the performance period. As of March 31, 2016, estimated unit payouts for outstanding nonvested performance unit awards ranged between 100% and 150%.

We granted 10,725 performance units during the three months ended March 31, 2016. Performance units granted in 2015 and during the three months ended March 31, 2016, vest over a three-year performance period ending December 31, 2018 and are payable in HEP common units. The number of units actually earned will be based on the growth of our distributable cash flow per common unit over the performance period, and can range from 50% to 150% of the target number of performance units granted. Although common units are not transferred to the recipients until the performance units vest, the recipients have distribution rights with respect to the common units from the date of grant.

- 13 -

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

A summary of performance unit activity and changes during the three months ended March 31, 2016, is presented below:

| Performance Units | Units |
|--|----------|
| Outstanding at January 1, 2016 (nonvested) | 45,494 |
| Granted | 10,725 |
| Vesting and transfer of common units to recipients | (26,157) |
| Outstanding at March 31, 2016 (Nonvested) | 30,062 |

The grant-date fair value of performance units vested and transferred to recipients during the three months ended March 31, 2016, was \$1.1 million. Based on the weighted average fair value of performance units outstanding at March 31, 2016, of \$0.9 million, there was \$0.7 million of total unrecognized compensation expense related to nonvested performance units, which is expected to be recognized over a weighted-average period of 2.4 years.

Note 6: Debt

Credit Agreement

In March 2016, we amended our senior secured revolving credit facility (the “Credit Agreement”) expiring in November 2018, increasing the size of the Credit Agreement from \$850 million to \$1.2 billion. The Credit Agreement is available to fund capital expenditures, investments, acquisitions, distribution payments and working capital and for general partnership purposes. It is also available to fund letters of credit up to a \$50 million sub-limit.

Our obligations under the Credit Agreement are collateralized by substantially all of our assets. Indebtedness under the Credit Agreement involves recourse to HEP Logistics Holdings, L.P. (“HEP Logistics”), our general partner, and is guaranteed by our material, wholly-owned subsidiaries. Any recourse to HEP Logistics would be limited to the extent of its assets, which other than its investment in us are not significant. We may prepay all loans at any time without penalty, except for payment of certain breakage and related costs.

The Credit Agreement imposes certain requirements on us with which we were in compliance as of March 31, 2016, 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 into a merger or consolidation, or sell assets; and covenants that require maintenance of a specified EBITDA to interest expense ratio, total debt to EBITDA ratio and senior debt to EBITDA ratio. If an event of default exists under the Credit Agreement, the lenders will be able to accelerate the maturity of the debt and exercise other rights and remedies.

Senior Notes

We have \$300 million in aggregate principal amount outstanding of 6.5% senior notes (the “6.5% Senior Notes”) maturing March 2020. The 6.5% Senior Notes are unsecured and impose certain restrictive covenants, with which we were in compliance as of March 31, 2016, 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 6.5% 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 at varying premiums over face value under the 6.5% Senior Notes.

Indebtedness under the 6.5% Senior Notes involves recourse to HEP Logistics, our general partner, and is guaranteed by our wholly-owned subsidiaries. However, any recourse to HEP Logistics would be limited to the extent of its assets, which, other than its investment in us, are not significant.

- 14 -

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

Long-term Debt

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

| | March 31, 2016 | December 31, 2015 |
|--|-------------------|----------------------|
| | (In thousands) | |
| Credit Agreement | | |
| Amount outstanding | \$765,000 | \$712,000 |
| 6.5% Senior Notes | | |
| Principal | 300,000 | 300,000 |
| Unamortized discount and debt issuance costs | (3,056) | (3,248) |
| | 296,944 | 296,752 |
| Total long-term debt | \$1,061,944 | \$1,008,752 |

Interest Rate Risk Management

We use interest rate swaps (derivative instruments) to manage our exposure to interest rate risk.

As of March 31, 2016, we have two interest rate swaps with identical terms that hedge our exposure to the cash flow risk caused by the effects of LIBOR changes on \$150 million of Credit Agreement advances. The swaps effectively convert \$150 million of our LIBOR based debt to fixed rate debt having an interest rate of 0.74% plus an applicable margin of 2.25% as of March 31, 2016, which equaled an effective interest rate of 2.99%. Both of these swap contracts mature in July 2017.

We have designated these interest rate swaps as cash flow hedges. Based on our assessment of effectiveness using the change in variable cash flows method, we have determined these interest rate swaps are effective in offsetting the variability in interest payments on \$150 million of our variable rate debt resulting from changes in LIBOR. Under hedge accounting, we adjust our cash flow hedges on a quarterly basis to their fair values with the offsetting fair value adjustments to accumulated other comprehensive income (loss). Also on a quarterly basis, we measure hedge effectiveness by comparing the present value of the cumulative change in the expected future interest to be paid or received on the variable leg of our swaps against the expected future interest payments on \$150 million of our variable rate debt. Any ineffectiveness is recorded directly to interest expense. As of March 31, 2016, we had no ineffectiveness on our cash flow hedges.

At March 31, 2016, we have accumulated other comprehensive loss of \$0.3 million that relates to our current cash flow hedging instruments. Approximately \$0.2 million will be transferred from accumulated other comprehensive loss into interest expense as interest is paid on the underlying swap agreement over the next twelve-month period, assuming interest rates remain unchanged.

Additional information on our interest rate swaps is as follows:

| Derivative Instrument | Balance Sheet Location (In thousands) | Fair Value | Location of Offsetting Balance | Offsetting Amount |
|-----------------------|---|------------|-----------------------------------|----------------------|
| March 31, 2016 | | | | |

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Interest rate swaps designated as cash flow hedging instrument:

| | | | | |
|--|--------------------------------|-----------|---|-----------|
| Variable-to-fixed interest rate swap contracts (\$150 million of LIBOR-based debt interest) | Other long-term liabilities | \$ (263) | Accumulated other comprehensive income | \$ (263) |
| | | \$ (263) | | \$ (263) |

December 31, 2015

Interest rate swaps designated as cash flow hedging instrument:

| | | | | |
|--|--------------------------------|--------|---|--------|
| Variable-to-fixed interest rate swap contract (\$150 million of LIBOR-based debt interest) | Other long-term assets | \$ 304 | Accumulated other comprehensive loss | \$ 304 |
| Variable-to-fixed interest rate swap contracts (\$155 million of LIBOR-based debt interest) | Other long-term liabilities | (114) | Accumulated other comprehensive income | (114) |
| | | \$ 190 | | \$ 190 |

- 15 -

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

Interest Expense and Other Debt Information

Interest expense consists of the following components:

| | Three Months Ended March 31, 2016 2015 (In thousands) | |
|---|--|----------|
| Interest on outstanding debt: | | |
| Credit Agreement, net of interest on interest rate swaps | \$5,006 | \$3,657 |
| 6.5% Senior Notes | 4,875 | 4,875 |
| Amortization of discount and deferred debt issuance costs | 593 | 436 |
| Commitment fees | 201 | 77 |
| Total interest incurred | 10,675 | 9,045 |
| Less capitalized interest | 140 | 277 |
| Net interest expense | \$10,535 | \$8,768 |
| Cash paid for interest | \$14,841 | \$13,400 |

Capital Lease Obligations

Our capital lease obligations, which relate to vehicle leases with initial terms of 33 to 36 months, are \$1.8 million as of both March 31, 2016 and December 31, 2015. The total cost of assets under capital leases was \$3.3 million and \$3.0 million as of March 31, 2016 and December 31, 2015, respectively, with accumulated depreciation of \$1.3 million and \$1.1 million as of March 31, 2016 and December 31, 2015, respectively. We include depreciation of capital leases in depreciation and amortization in our consolidated statements of income.

Note 7: Significant Customers

All revenues are domestic revenues, of which 89% are currently generated from our two largest customers: HFC and Alon.

The following table presents the percentage of total revenues generated by each of these customers:

| | Three Months Ended March 31, 2016 2015 | |
|------|--|------|
| HFC | 81 % | 81 % |
| Alon | 8 % | 9 % |

Note 8: Related Party Transactions

We serve HFC's refineries under long-term pipeline, terminal and tankage throughput agreements, and refinery processing unit tolling agreements expiring from 2019 to 2030. Under these agreements, HFC agrees to transport,

store and process throughput volumes of refined product, crude oil and feedstocks on our pipelines, terminals, tankage, loading rack facilities and refinery processing units that result in minimum annual payments to us. These minimum annual payments or revenues are subject to annual rate adjustments on July 1st each year based on the Producer Price Index (“PPI”) or Federal Energy Regulatory Commission (“FERC”) index. As of March 31, 2016, these agreements with HFC require minimum annualized payments to us of \$263.7 million.

If HFC fails to meet its minimum volume commitments under the agreements in any quarter, it will be required to pay us the amount of any shortfall in cash by the last day of the month following the end of the quarter. Under certain of these agreements, a shortfall payment may be applied as a credit in the following four quarters after its minimum obligations are met.

Under certain provisions of an omnibus agreement we have with HFC (the “Omnibus Agreement”), we pay HFC an annual administrative fee (currently \$2.5 million) for the provision by HFC or its affiliates of various general and administrative services to us. This fee does not include the salaries of personnel employed by HFC who perform services for us on behalf of HLS or the cost of their employee benefits, which are charged to us separately by HFC. Also, we reimburse HFC and its affiliates for direct expenses they incur on our behalf.

- 16 -

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

Related party transactions with HFC are as follows:

Revenues received from HFC were \$82.8 million and \$72.3 million for the three months ended March 31, 2016 and 2015, respectively.

HFC charged us general and administrative services under the Omnibus Agreement of \$0.6 million for each of the three months ended March 31, 2016 and 2015.

We reimbursed HFC for costs of employees supporting our operations of \$9.8 million and \$8.8 million for the three months ended March 31, 2016 and 2015, respectively.

HFC reimbursed us \$1.8 million and \$2.6 million for the three months ended March 31, 2016 and 2015, respectively, for certain reimbursable costs and capital projects.

We distributed \$24.5 million and \$21.6 million for the three months ended March 31, 2016 and 2015, respectively, to HFC as regular distributions on its common units and general partner interest, including general partner incentive distributions.

Accounts receivable from HFC were \$33.1 million and \$32.5 million at March 31, 2016, and December 31, 2015, respectively.

Accounts payable to HFC were \$6.2 million and \$11.6 million at March 31, 2016, and December 31, 2015, respectively.

Revenues for the three months ended March 31, 2016 and 2015, include \$5.2 million and \$5.6 million, respectively, of shortfall payments billed in 2015 and 2014, respectively, as HFC did not exceed its minimum volume commitment in any of the subsequent four quarters. Deferred revenue in the consolidated balance sheets at March 31, 2016, and December 31, 2015, includes \$1.5 million and \$6.4 million, respectively, relating to certain shortfall billings. It is possible that HFC may not exceed its minimum obligations to receive credit for any of the \$1.5 million deferred at March 31, 2016.

On February 22, 2016, HFC obtained a 50% membership interest in Osage in a non-monetary exchange, whereby a subsidiary of Magellan will provide terminalling services for all HFC products originating in Artesia, New Mexico that require terminalling in or through El Paso, Texas. Concurrent with this transaction, we entered into a non-monetary exchange with HFC, whereby we received HFC's interest in Osage in exchange for our El Paso terminal. See Note 1 for a description of this transaction.

On March 31, 2016, we acquired crude oil tanks located at HFC's Tulsa refinery from an affiliate of Plains All American Pipeline, L.P. for \$39.5 million. See Note 1 for a description of this transaction.

Note 9: Partners' Equity

As of March 31, 2016, HFC held 22,380,030 of our common units and the 2% general partner interest, which together constituted a 39% ownership interest in us. Additionally, HFC owned all incentive distribution rights in us.

Allocations of Net Income

Net income attributable to HEP is allocated between limited partners and the general partner interest in accordance with the provisions of the partnership agreement. HEP net income allocated to the general partner includes incentive distributions that are declared subsequent to quarter end. After the amount of incentive distributions is allocated to the general partner, the remaining net income attributable to HEP is allocated to the partners based on their weighted-average ownership percentage during the period.

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

The following table presents the allocation of the general partner interest in net income for the periods presented below:

| | Three Months Ended March 31, 2016 2015 (In thousands) | |
|--|---|---------|
| General partner interest in net income | \$413 | \$246 |
| General partner incentive distribution | 11,473 | 9,361 |
| Total general partner interest in net income | \$11,886 | \$9,607 |

Cash Distributions

Our general partner, HEP Logistics, is entitled to incentive distributions if the amount we distribute with respect to any quarter exceeds specified target levels.

On April 22, 2016, we announced our cash distribution for the first quarter of 2016 of \$0.575 per unit. The distribution is payable on all common and general partner units and will be paid May 13, 2016, to all unitholders of record on May 2, 2016.

The following table presents the allocation of our regular quarterly cash distributions to the general and limited partners for the periods in which they apply. Our distributions are declared subsequent to quarter end; therefore, the amounts presented do not reflect distributions paid during the periods presented below.

| | Three Months Ended March 31, 2016 2015 (In thousands, except per unit data) | |
|---|--|----------|
| General partner interest in distribution | \$948 | \$860 |
| General partner incentive distribution | 11,473 | 9,361 |
| Total general partner distribution | 12,421 | 10,221 |
| Limited partner distribution | 33,728 | 31,528 |
| Total regular quarterly cash distribution | \$46,149 | \$41,749 |
| Cash distribution per unit applicable to limited partners | \$0.5750 | \$0.5375 |

As a master limited partnership, we distribute our available cash, which historically has exceeded our net income attributable to HEP because depreciation and amortization expense represents a non-cash charge against income. The result is a decline in our partners' equity since our regular quarterly distributions have exceeded our quarterly net income attributable to HEP. Additionally, if the asset contributions and acquisitions from HFC had occurred while we were not a consolidated variable interest entity of HFC, our acquisition cost in excess of HFC's historical basis in the transferred assets would have been recorded in our financial statements at the time of acquisition as increases to our properties and equipment and intangible assets instead of decreases to our partners' equity.

Note 10: Environmental

We incurred no expenses for the three months ended March 31, 2016 and \$4.2 million for the three months ended March 31, 2015, for environmental remediation obligations. The accrued environmental liability, net of expected recoveries from indemnifying parties, reflected in our consolidated balance sheets was \$7.4 million and \$7.7 million at March 31, 2016, and December 31, 2015, respectively, of which \$5.8 million and \$6.1 million, respectively, were classified as other long-term liabilities. These accruals include remediation and monitoring costs expected to be incurred over an extended period of time.

Under the Omnibus Agreement and certain transportation agreements and purchase agreements with HFC, HFC has agreed to indemnify us, subject to certain monetary and time limitations, for environmental noncompliance and remediation liabilities associated with certain assets transferred to us from HFC and occurring or existing prior to the date of such transfers. As of March 31, 2016, and December 31, 2015, our accrued environmental liability included \$1.0 million and \$6.4 million, respectively, for HFC indemnified liabilities, and other assets included equal and offsetting balances representing amounts due from HFC related to indemnifications for environmental remediation liabilities.

- 18 -

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

Note 11: Contingencies

We are a party to various legal and regulatory proceedings, none of which we believe will have a material adverse impact on our financial condition, results of operation or cash flows.

Note 12: Supplemental Guarantor/Non-Guarantor Financial Information

Obligations of HEP (“Parent”) under the Senior Notes have been jointly and severally guaranteed by each of its direct and indirect 100% owned subsidiaries (“Guarantor Subsidiaries”). These guarantees are full and unconditional, subject to certain customary release provisions. These circumstances include (i) when a Guarantor Subsidiary is sold or sells all or substantially all of its assets, (ii) when a Guarantor Subsidiary is declared “unrestricted” for covenant purposes, (iii) when a Guarantor Subsidiary’s guarantee of other indebtedness is terminated or released and (iv) when the requirements for legal defeasance or covenant defeasance or to discharge the Senior Notes have been satisfied.

The following financial information presents condensed consolidating balance sheets, statements of comprehensive income, and statements of cash flows of the Parent, the Guarantor Subsidiaries and the Non-Guarantor Subsidiaries. The information has been presented as if the Parent accounted for its ownership in the Guarantor Subsidiaries, and the Guarantor Restricted Subsidiaries accounted for the ownership of the Non-Guarantor Non-Restricted Subsidiaries, using the equity method of accounting.

HOLLY ENERGY PARTNERS, L.P.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited) Continued

Condensed Consolidating Balance Sheet

| March 31, 2016 | Parent | Guarantor Restricted Subsidiaries | Non-Guarantor Non-Restricted Subsidiaries | Eliminations | Consolidated |
|----------------------------------|----------------|---|---|--------------|----------------|
| | (In thousands) | | | | |
| ASSETS | | | | | |
| Current assets: | | | | | |
| Cash and cash equivalents | \$2 | \$ 1,003 | \$ 8,029 | \$ — | \$ 9,034 |
| Accounts receivable | — | 36,505 | 4,721 | (170 |) 41,056 |
| Prepaid and other current assets | 199 | 3,766 | 1,216 | — | 5,181 |
| Total current assets | 201 | 41,274 | 13,966 | (170 |) 55,271 |
| | | | | | |
| Properties and equipment, net | — | 672,825 | 379,947 | — | 1,052,772 |
| Investment in subsidiaries | 586,328 | 288,721 | — | (875,049 |) — |
| Transportation agreements, net | — | 72,067 | — | — | 72,067 |
| Goodwill | — | 256,498 | — | — | 256,498 |
| Equity method investments | — | 124,134 | — | — | 124,134 |
| Other assets | 658 | 11,161 | — | — | 11,819 |
| Total assets | \$587,187 | \$ 1,466,680 | \$ 393,913 | \$ (875,219 |) \$ 1,572,561 |
| | | | | | |
| LIABILITIES AND EQUITY | | | | | |
| Current liabilities: | | | | | |
| Accounts payable | \$— | \$ 12,124 | \$ 6,526 | \$ (170 |) \$ 18,480 |
| Accrued interest | 1,625 | 347 | — | — | 1,972 |
| Deferred revenue | — | 6,736 | 314 | — | 7,050 |
| Accrued property taxes | — | 2,210 | 1,897 | — | 4,107 |
| Other current liabilities | 213 | 2,692 | 40 | — | 2,945 |
| Total current liabilities | 1,838 | 24,109 | 8,777 | (170 |) 34,554 |
| | | | | | |
| Long-term debt | 296,944 | 765,000 | — | — | 1,061,944 |
| Other long-term liabilities | 227 | 15,995 | 175 | — | 16,397 |
| Deferred revenue | — | 39,441 | — | — | 39,441 |
| Class B unit | — | 35,807 | — | — | 35,807 |
| Equity - partners | 288,178 | 586,328 | 384,961 | (971,289 |) 288,178 |
| Equity - noncontrolling interest | — | — | — | 96,240 | 96,240 |
| Total liabilities and equity | \$587,187 | \$ 1,466,680 | \$ 393,913 | \$ (875,219 |) \$ 1,572,561 |

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

Condensed Consolidating Balance Sheet

| December 31, 2015 ⁽¹⁾ | Parent | Guarantor Restricted Subsidiaries | Non-Guarantor Non-Restricted Subsidiaries | Eliminations | Consolidated |
|----------------------------------|----------------|---|---|--------------|----------------|
| | (In thousands) | | | | |
| ASSETS | | | | | |
| Current assets: | | | | | |
| Cash and cash equivalents | \$2 | \$ 5,452 | \$ 9,559 | \$ — | \$ 15,013 |
| Accounts receivable | — | 35,558 | 5,715 | (198 |) 41,075 |
| Prepaid and other current assets | 174 | 3,634 | 1,246 | — | 5,054 |
| Total current assets | 176 | 44,644 | 16,520 | (198 |) 61,142 |
| | | | | | |
| Properties and equipment, net | — | 687,336 | 371,843 | — | 1,059,179 |
| Investment in subsidiaries | 600,563 | 283,287 | — | (883,850 |) — |
| Transportation agreements, net | — | 73,805 | — | — | 73,805 |
| Goodwill | — | 256,498 | — | — | 256,498 |
| Equity method investments | — | 79,438 | — | — | 79,438 |
| Other assets | 642 | 13,061 | — | — | 13,703 |
| Total assets | \$601,381 | \$ 1,438,069 | \$ 388,363 | \$ (884,048 |) \$ 1,543,765 |
| | | | | | |
| LIABILITIES AND EQUITY | | | | | |
| Current liabilities: | | | | | |
| Accounts payable | \$— | \$ 19,448 | \$ 3,333 | \$ (198 |) \$ 22,583 |
| Accrued interest | 6,500 | 252 | — | — | 6,752 |
| Deferred revenue | — | 6,010 | 6,006 | — | 12,016 |
| Accrued property taxes | — | 2,627 | 1,137 | — | 3,764 |
| Other current liabilities | 7 | 3,802 | — | — | 3,809 |
| Total current liabilities | 6,507 | 32,139 | 10,476 | (198 |) 48,924 |
| | | | | | |
| Long-term debt | 296,752 | 712,000 | — | — | 1,008,752 |
| Other long-term liabilities | 210 | 20,363 | 171 | — | 20,744 |
| Deferred revenue | — | 39,063 | — | — | 39,063 |
| Class B unit | — | 33,941 | — | — | 33,941 |
| Equity - partners | 297,912 | 600,563 | 377,716 | (978,279 |) 297,912 |
| Equity - noncontrolling interest | — | — | — | 94,429 | 94,429 |
| Total liabilities and equity | \$601,381 | \$ 1,438,069 | \$ 388,363 | \$ (884,048 |) \$ 1,543,765 |

(1) Retrospectively adjusted as described in Note 1.

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

Condensed Consolidating Statement of Comprehensive Income

| Three Months Ended March 31, 2016 | Parent | Guarantor Restricted Subsidiaries | Non-Guarantor Non-restricted Subsidiaries | Eliminations | Consolidated |
|---|----------------|---|---|--------------|--------------|
| | (In thousands) | | | | |
| Revenues: | | | | | |
| Affiliates | \$ — | \$ 72,252 | \$ 10,594 | \$ — | \$ 82,846 |
| Third parties | — | 10,732 | 8,432 | — | 19,164 |
| | — | 82,984 | 19,026 | — | 102,010 |
| Operating costs and expenses: | | | | | |
| Operations (exclusive of depreciation and amortization) | — | 23,891 | 3,031 | — | 26,922 |
| Depreciation and amortization | | 12,793 | 3,758 | — | 16,551 |
| General and administrative | 1,165 | 1,926 | — | — | 3,091 |
| | 1,165 | 38,610 | 6,789 | — | 46,564 |
| Operating income (loss) | (1,165) | 44,374 | 12,237 | — | 55,446 |
| Equity in earnings of subsidiaries | 48,990 | 9,184 | — | (58,174) | — |
| Equity in earnings of equity method investments | — | 2,765 | — | — | 2,765 |
| Interest expense | (5,067) | (5,468) | — | — | (10,535) |
| Interest income | — | 105 | 7 | — | 112 |
| Other income (expense) | — | (9) | 1 | — | (8) |
| | 43,923 | 6,577 | 8 | (58,174) | (7,666) |
| Income (loss) before income taxes | 42,758 | 50,951 | 12,245 | (58,174) | 47,780 |
| State income tax expense | — | (95) | — | — | (95) |
| Net income (loss) | 42,758 | 50,856 | 12,245 | (58,174) | 47,685 |
| Allocation of net (income) attributable to noncontrolling interests | — | — | — | (4,927) | (4,927) |
| Net income (loss) attributable to Holly Energy Partners | 42,758 | 50,856 | 12,245 | (63,101) | 42,758 |
| Other comprehensive income (loss) | (453) | (453) | — | 453 | (453) |
| Comprehensive income (loss) attributable to Holly Energy Partners | \$ 42,305 | \$ 50,403 | \$ 12,245 | \$ (62,648) | \$ 42,305 |

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

Condensed Consolidating Statement of Comprehensive Income

| Three Months Ended March 31, 2015 ⁽¹⁾ | Parent | Guarantor Restricted Subsidiaries | Non-Guarantor Non-Restricted Subsidiaries | Eliminations | Consolidated |
|---|----------------|---|---|--------------|--------------|
| | (In thousands) | | | | |
| Revenues: | | | | | |
| Affiliates | \$— | \$ 63,056 | \$ 9,224 | \$ (25) | \$ 72,255 |
| Third parties | — | 11,387 | 6,114 | — | 17,501 |
| | — | 74,443 | 15,338 | (25) | 89,756 |
| Operating costs and expenses: | | | | | |
| Operations (exclusive of depreciation and amortization) | — | 25,630 | 2,460 | (25) | 28,065 |
| Depreciation and amortization | — | 11,066 | 3,732 | — | 14,798 |
| General and administrative | 1,063 | 2,227 | — | — | 3,290 |
| | 1,063 | 38,923 | 6,192 | (25) | 46,153 |
| Operating income (loss) | (1,063) | 35,520 | 9,146 | — | 43,603 |
| Equity in earnings of subsidiaries | 37,730 | 6,860 | — | (44,590) | — |
| Equity in earnings of equity method investments | — | 734 | — | — | 734 |
| Interest expense | (5,067) | (3,701) | — | — | (8,768) |
| Gain on sale of assets | — | 159 | — | — | 159 |
| | 32,663 | 4,052 | — | (44,590) | (7,875) |
| Income (loss) before income taxes | 31,600 | 39,572 | 9,146 | (44,590) | 35,728 |
| State income tax expense | — | (101) | — | — | (101) |
| Net income (loss) | 31,600 | 39,471 | 9,146 | (44,590) | 35,627 |
| Allocation of net (income) attributable to noncontrolling interests | — | — | — | (4,027) | (4,027) |
| Net income (loss) attributable to Holly Energy Partners | 31,600 | 39,471 | 9,146 | (48,617) | 31,600 |
| Other comprehensive income (loss) | (749) | (749) | — | 749 | (749) |
| Comprehensive income (loss) attributable to Holly Energy Partners | \$30,851 | \$ 38,722 | \$ 9,146 | \$ (47,868) | \$ 30,851 |

(1) Retrospectively adjusted as described in Note 1.

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

Condensed Consolidating Statement of Cash Flows

| Three Months Ended March 31, 2016 | Parent | Guarantor Restricted Subsidiaries | Non-Guarantor Non-Restricted Subsidiaries | Eliminations | Consolidated |
|---|----------------|---|---|--------------|--------------|
| | (In thousands) | | | | |
| Cash flows from operating activities | \$(10,084) | \$ 48,712 | \$ 13,424 | \$ (3,750) | \$ 48,302 |
| Cash flows from investing activities | | | | | |
| Additions to properties and equipment | — | (7,919) | (9,954) | — | (17,873) |
| Proceeds from sale of assets | — | 12 | — | — | 12 |
| Distributions in excess of equity in earnings of equity investments | — | 99 | — | — | 99 |
| | — | (7,808) | (9,954) | — | (17,762) |
| Cash flows from financing activities | | | | | |
| Net borrowings under credit agreement | — | 53,000 | — | — | 53,000 |
| Net intercompany financing activities | 53,751 | (53,751) | — | — | — |
| Contribution from general partners | 32,455 | (32,455) | — | — | — |
| Distributions to HEP unitholders | (44,960) | — | — | — | (44,960) |
| Distributions to HFC for Tulsa Tanks | (30,378) | (9,122) | — | — | (39,500) |
| Contributions from HFC for Tulsa Tanks | — | 99 | — | — | 99 |
| Distributions to noncontrolling interests | — | — | (5,000) | 3,750 | (1,250) |
| Purchase of units for incentive grants | (784) | — | — | — | (784) |
| Deferred financing cost | — | (2,964) | — | — | (2,964) |
| Other | — | (160) | — | — | (160) |
| | 10,084 | (45,353) | (5,000) | 3,750 | (36,519) |
| Cash and cash equivalents | | | | | |
| Increase (decrease) for the period | — | (4,449) | (1,530) | — | (5,979) |
| Beginning of period | 2 | 5,452 | 9,559 | — | 15,013 |
| End of period | \$2 | \$ 1,003 | \$ 8,029 | \$ — | \$ 9,034 |

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

Condensed Consolidating Statement of Cash Flows

| Three Months Ended March 31, 2015 ⁽¹⁾ | Parent | Guarantor Restricted Subsidiaries | Non-Guarantor Non-Restricted Subsidiaries | Eliminations | Consolidated |
|---|----------------|---|---|--------------|--------------|
| | (In thousands) | | | | |
| Cash flows from operating activities | \$ (9,873) | \$ 63,029 | \$ 8,328 | \$ (692) | \$ 60,792 |
| Cash flows from investing activities | | | | | |
| Additions to properties and equipment | — | (23,919) | (308) | — | (24,227) |
| Purchase of El Dorado crude tanks | — | (27,500) | — | — | (27,500) |
| Proceeds from sale of assets | — | 218 | — | — | 218 |
| Distributions from noncontrolling interest | — | 3,058 | — | (3,058) | — |
| Distributions in excess of equity in earnings of equity investments | — | 16 | — | — | 16 |
| | — | (48,127) | (308) | (3,058) | (51,493) |
| Cash flows from financing activities | | | | | |
| Net repayments under credit agreement | — | 23,000 | — | — | 23,000 |
| Net intercompany financing activities | 50,985 | (50,985) | — | — | — |
| Contributions from HFC for El Dorado Operating acquisition | — | 12,563 | — | — | 12,563 |
| Distributions to HEP unitholders | (40,865) | — | — | — | (40,865) |
| Contribution from HFC for Tulsa tank acquisition | — | 472 | — | — | 472 |
| Distributions to noncontrolling interests | — | — | (5,000) | 3,750 | (1,250) |
| Purchase of units for incentive grants | (247) | — | — | — | (247) |
| | 9,873 | (14,950) | (5,000) | 3,750 | (6,327) |
| Cash and cash equivalents | | | | | |
| Increase (decrease) for the period | — | (48) | 3,020 | — | 2,972 |
| Beginning of period | 2 | 2,828 | — | — | 2,830 |
| End of period | \$ 2 | \$ 2,780 | \$ 3,020 | \$ — | \$ 5,802 |

(1) Retrospectively adjusted as described in Note 1.

Table of Contentsril 19,

HOLLY ENERGY PARTNERS, L.P.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

This Item 2, including but not limited to the sections under "Results of Operations" and "Liquidity and Capital Resources," contains forward-looking statements. See "Forward-Looking Statements" at the beginning of Part I of this Quarterly Report on Form 10-Q. In this document, the words "we," "our," "ours" and "us" refer to Holly Energy Partners, L. P. ("HEP") and its consolidated subsidiaries or to HEP or an individual subsidiary and not to any other person.

OVERVIEW

HEP is a Delaware limited partnership. We own and operate petroleum product and crude oil pipelines, terminal, tankage and loading rack facilities and refinery processing units that support the refining and marketing operations of HollyFrontier Corporation ("HFC") in the Mid-Continent, Southwest and Rocky Mountain regions of the United States and Alon USA, Inc.'s ("Alon") refinery in Big Spring, Texas. HFC owns a 39% interest in us, including the 2% general partnership interest. Additionally, we own a 75% interest in UNEV Pipeline, LLC ("UNEV"), the owner of a pipeline running from Woods Cross, Utah to Las Vegas, Nevada (the "UNEV Pipeline") and product terminals, a 50% interest in Osage Pipe Line Company, LLC, the owner of a crude oil pipeline running from Cushing, Oklahoma to El Dorado, Kansas ("Osage Pipeline"), a 50% interest in Frontier Pipeline Company, the owner of a crude oil pipeline running from Casper, Wyoming to Frontier Station, Utah (the "Frontier Pipeline") and a 25% interest in SLC Pipeline, LLC, the owner of a crude oil pipeline (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, providing other services at our storage tanks and terminals and charging a tolling fee per barrel or thousand standard cubic feet of feedstock throughput in our refinery processing units. We do not take ownership of products that we transport, terminal or store, and therefore, we are not directly exposed to changes in commodity prices.

We believe the long-term growth of global refined product demand and US crude production should support high utilization rates for the refineries we serve, which in turn will support volumes in our product pipelines, crude gathering system and terminals.

UNEV Pipeline Interest Acquisition

Under the terms of the transaction to acquire HFC's 75% interest in UNEV in 2012, we issued to HFC a Class B unit comprising a noncontrolling equity interest in a wholly-owned subsidiary subject to redemption to the extent that HFC is entitled to a 50% interest in our share of annual UNEV earnings before interest, income taxes, depreciation, and amortization above \$30 million beginning July 1, 2016, and ending in June 2032, subject to certain limitations. However, to the extent earnings thresholds are not achieved, no redemption payments are required. Contemporaneously with this transaction, HEP Logistics Holdings, L.P. ("HEP Logistics") (our general partner) agreed to forego its right to incentive distributions of up to \$1.25 million per quarter over twelve consecutive quarterly periods following the closing of the transaction and up to an additional four quarters if HFC's Woods Cross Refinery expansion did not attain certain thresholds. We expect HEP Logistics' waiver of its right to incentive distributions of \$1.25 million per quarter to end in the third quarter of 2016. In connection with the transaction, we entered into 15-year throughput agreements with shippers, which currently require minimum annual revenue commitments to us of \$30 million.

Acquisitions

On March 31, 2016, we acquired crude oil tanks located at HFC's Tulsa refinery from an affiliate of Plains All American Pipeline, L.P. for \$39.5 million. In connection with this transaction, we expect to enter into a 10-year throughput agreement containing minimum quarterly throughput commitments from HFC that provide minimum

annualized revenues of \$6.1 million.

On February 22, 2016, HFC obtained a 50% membership interest in Osage Pipe Line Company, LLC (“Osage”) in a non-monetary exchange for a 20-year terminalling services agreement, whereby a subsidiary of Magellan Midstream Partners (“Magellan”) will provide terminalling services for all HFC products originating in Artesia, New Mexico that require terminalling in or through El Paso, Texas. Osage is the owner of the Osage Pipeline, a 135-mile pipeline that transports crude oil from Cushing, Oklahoma to HFC’s El Dorado Refinery in Kansas and also has a connection to the Jayhawk pipeline that services the CHS Inc. refinery in McPherson, Kansas. The Osage Pipeline is the primary pipeline that supplies HFC’s El Dorado Refinery with crude oil.

Concurrent with this transaction, we entered into a non-monetary exchange with HFC, whereby we received HFC’s interest in Osage in exchange for our El Paso terminal. Under this exchange, we have also agreed to build two connections on our south products pipeline system that will permit HFC access to Magellan’s El Paso terminal. Effective upon the closing of this exchange, we are the named operator of the Osage Pipeline and are working to transition into that role. Since we are a consolidated variable

- 26 -

Table of Contentsril 19,

interest entity of HFC, this transaction will be recorded as a transfer between entities under common control and reflect HFC's carrying basis of its 50% membership interest in Osage of \$44.0 million offset by our carrying basis in the El Paso terminal of \$12.0 million with the difference treated as a contribution from HFC.

On November 1, 2015, we acquired from HollyFrontier 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 was recorded as a transfer between entities under common control and reflected HFC's carrying basis in El Dorado Operating's assets and liabilities.

Agreements with HFC and Alon

We serve HFC's refineries under long-term pipeline, terminal and tankage throughput agreements and refinery processing unit tolling agreements expiring from 2019 to 2030. Under these agreements, HFC has agreed to transport, store and process throughput volumes of refined product, crude oil and feedstocks on our pipelines, terminal, tankage, loading rack facilities and refinery processing units that result in minimum annual payments to us. These minimum annual payments or revenues are subject to annual rate adjustments on July 1st each year, based on the Producer Price Index ("PPI") or Federal Energy Regulatory Commission ("FERC") index. As of March 31, 2016, these agreements with HFC require minimum annualized payments to us of \$263.7 million.

If HFC fails to meet its minimum volume commitments under the agreements in any quarter, it will be required to pay us the amount of any shortfall in cash by the last day of the month following the end of the quarter. Under certain of the agreements, a shortfall payment may be applied as a credit in the following four quarters after minimum obligations are met.

We also have a pipelines and terminals agreement with Alon expiring in 2020 under which Alon has agreed to transport on our pipelines and throughput through our terminals volumes of refined products that result in a minimum level of annual revenue that is also subject to annual tariff rate adjustments. We also have a capacity lease agreement under which we lease Alon space on our Orla to El Paso pipeline for the shipment of refined product. The terms under this agreement expire beginning in 2018 through 2022. As of March 31, 2016, these agreements with Alon require minimum annualized payments to us of \$32.3 million.

A significant reduction in revenues under these agreements could have a material adverse effect on our results of operations.

Under certain provisions of an omnibus agreement we have with HFC ("Omnibus Agreement"), we pay HFC an annual administrative fee, currently \$2.5 million, for the provision by HFC or its affiliates of various general and administrative services to us. This fee does not include the salaries of personnel employed by HFC who perform services for us on behalf of Holly Logistic Services, L.L.C. ("HLS"), or the cost of their employee benefits, which are separately charged to us by HFC. We also reimburse HFC and its affiliates for direct expenses they incur on our behalf.

Under HLS's Secondment Agreement with HFC, certain employees of HFC are seconded to HLS to provide operational and maintenance services for certain of our processing, refining, pipeline and tankage assets at the El Dorado, Cheyenne and Tulsa refineries, and HLS reimburses HFC for its prorated portion of the wages, benefits, and other costs of these employees for our benefit.

We have a long-term strategic relationship with HFC. Our current growth plan is to continue to pursue purchases of logistic and other assets at HFC's existing refining locations in New Mexico, Utah, Oklahoma, Kansas and Wyoming. We also expect to work with HFC on logistic asset acquisitions that support HFC's refinery acquisition strategies. Furthermore, we plan to continue to pursue third-party logistic asset acquisitions that are accretive to our unitholders and increase the diversity of our revenues.

- 27 -

Table of Contentsril 19,

RESULTS OF OPERATIONS (Unaudited)

Income, Distributable Cash Flow and Volumes

The following tables present income, distributable cash flow and volume information for the three months ended March 31, 2016 and 2015.

| | Three Months Ended March 31, 2016 2015 | | Change from 2015 |
|--|---|----------|------------------------|
| | (In thousands, except per unit data) | | |
| Revenues: | | | |
| Pipelines: | | | |
| Affiliates—refined product pipelines | \$25,182 | \$22,541 | \$2,641 |
| Affiliates—intermediate pipelines | 7,413 | 6,862 | 551 |
| Affiliates—crude pipelines | 17,491 | 16,994 | 497 |
| | 50,086 | 46,397 | 3,689 |
| Third parties—refined product pipelines | 14,766 | 13,723 | 1,043 |
| | 64,852 | 60,120 | 4,732 |
| Terminals, tanks and loading racks: | | | |
| Affiliates | 28,253 | 25,858 | 2,395 |
| Third parties | 4,398 | 3,778 | 620 |
| | 32,651 | 29,636 | 3,015 |
| Affiliates—refinery processing units | 4,507 | — | 4,507 |
| Total revenues | 102,010 | 89,756 | 12,254 |
| Operating costs and expenses: | | | |
| Operations (exclusive of depreciation and amortization) | 26,922 | 28,065 | (1,143) |
| Depreciation and amortization | 16,551 | 14,798 | 1,753 |
| General and administrative | 3,091 | 3,290 | (199) |
| | 46,564 | 46,153 | 411 |
| Operating income | 55,446 | 43,603 | 11,843 |
| Other income (expense): | | | |
| Equity in earnings of equity method investments | 2,765 | 734 | 2,031 |
| Interest expense, including amortization | (10,535) | (8,768) | (1,767) |
| Interest income | 112 | — | 112 |
| Gain on sale of assets | — | 159 | (159) |
| Other | (8) | — | (8) |
| | (7,666) | (7,875) | 209 |
| Income before income taxes | 47,780 | 35,728 | 12,052 |
| State income tax expense | (95) | (101) | 6 |
| Net income | 47,685 | 35,627 | 12,058 |
| Allocation of net income attributable to noncontrolling interests | (4,927) | (4,027) | (900) |
| Net income attributable to Holly Energy Partners | 42,758 | 31,600 | 11,158 |
| General partner interest in net income, including incentive distributions ⁽¹⁾ | (11,886) | (9,607) | (2,279) |
| Limited partners' interest in net income | \$30,872 | \$21,993 | \$8,879 |
| Limited partners' earnings per unit—basic and diluted ⁽¹⁾ | \$0.52 | \$0.37 | \$0.15 |

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| | | | |
|--|-----------|-----------|----------|
| Weighted average limited partners' units outstanding | 58,657 | 58,657 | — |
| EBITDA ⁽²⁾ | \$69,827 | \$55,267 | \$14,560 |
| Distributable cash flow ⁽³⁾ | \$55,365 | \$45,890 | \$9,475 |
| Volumes (bpd) | | | |
| Pipelines: | | | |
| Affiliates—refined product pipelines | 132,430 | 115,430 | 17,000 |
| Affiliates—intermediate pipelines | 137,410 | 138,073 | (663) |
| Affiliates—crude pipelines | 287,433 | 282,705 | 4,728 |
| | 557,273 | 536,208 | 21,065 |
| Third parties—refined product pipelines | 78,334 | 71,420 | 6,914 |
| | 635,607 | 607,628 | 27,979 |
| Terminals and loading racks: | | | |
| Affiliates | 385,538 | 323,150 | 62,388 |
| Third parties | 81,327 | 73,988 | 7,339 |
| | 466,865 | 397,138 | 69,727 |
| Affiliates—refinery processing units | 42,442 | — | 42,442 |
| Total for pipelines and terminal assets (bpd) | 1,144,914 | 1,004,766 | 140,148 |

- 28 -

Table of Contentsril 19,

| | March 31, 2016 | December 31, 2015 |
|---------------------------------|-------------------|----------------------|
| | (In thousands) | |
| Balance Sheet Data | | |
| Cash and cash equivalents | \$9,034 | \$ 15,013 |
| Working capital | \$20,717 | \$ 12,218 |
| Total assets | \$1,572,561 | \$ 1,543,765 |
| Long-term debt | \$1,061,944 | \$ 1,008,752 |
| Partners' equity ⁽⁵⁾ | \$288,178 | \$ 297,912 |

Net income attributable to HEP is allocated between limited partners and the general partner interest in accordance with the provisions of the partnership agreement. HEP net income allocated to the general partner includes (1) incentive distributions that are declared subsequent to quarter end. After the amount of incentive distributions is allocated to the general partner, the remaining net income attributable to HEP is allocated to the partners based on their weighted average ownership percentage during the period.

Earnings before interest, taxes, depreciation and amortization ("EBITDA") is calculated as net income attributable to Holly Energy Partners plus (i) interest expense and loss on early extinguishment of debt, net of interest income, (ii) state income tax and (iii) depreciation and amortization. EBITDA is not a calculation based upon generally accepted accounting principles ("GAAP"). However, the amounts included in the EBITDA calculation are derived from amounts included in our consolidated financial statements operations. EBITDA should not be considered as (2) an alternative to net income attributable to Holly Energy Partners or operating income, as an indication of our operating performance or as an alternative to operating cash flow as a measure of liquidity. EBITDA is not necessarily comparable to similarly titled measures of other companies. EBITDA is presented here because it is a widely used financial indicator used by investors and analysts to measure performance. EBITDA is also used by our management for internal analysis and as a basis for compliance with financial covenants. Set forth below is our calculation of EBITDA.

| | Three Months Ended March 31, 2016 2015 (In thousands) | |
|---|---|----------|
| Net income attributable to Holly Energy Partners | \$42,758 | \$31,600 |
| Add (subtract): | | |
| Interest expense | 9,942 | 8,332 |
| Interest income | (112) | — |
| Amortization of discount and deferred debt issuance costs | 593 | 436 |
| State income tax expense | 95 | 101 |
| Depreciation and amortization | 16,551 | 14,798 |
| EBITDA | \$69,827 | \$55,267 |

(3) Distributable cash flow is not a calculation based upon GAAP. However, the amounts included in the calculation are derived from amounts presented in our consolidated financial statements, with the general exceptions of maintenance capital expenditures. Distributable cash flow should not be considered in isolation or as an alternative to net income or operating income as an indication of our operating performance or as an alternative to operating cash flow as a measure of liquidity. Distributable cash flow is not necessarily comparable to similarly titled measures of other companies. Distributable cash flow is presented here because it is a widely accepted financial indicator used by investors to compare partnership performance. It is also used by management for internal

analysis and for our performance units. We believe that this measure provides investors an enhanced perspective of the operating performance of our assets and the cash our business is generating. Set forth below is our calculation of distributable cash flow.

- 29 -

Table of Contentsril 19,

| | Three Months Ended March 31, 2016 (In thousands) | 2015 |
|--|--|-----------|
| Net income attributable to Holly Energy Partners | \$ 42,758 | \$ 31,600 |
| Add (subtract): | | |
| Depreciation and amortization | 16,551 | 14,798 |
| Amortization of discount and deferred debt issuance costs | 593 | 436 |
| Increase (decrease) in deferred revenue related to minimum revenue commitments | (3,658) | (3,550) |
| Maintenance capital expenditures ⁽⁴⁾ | (1,661) | (1,649) |
| Increase (decrease) in environmental liability | (328) | 3,856 |
| Increase (decrease) in reimbursable deferred revenue | (528) | (544) |
| Other non-cash adjustments | 1,638 | 943 |
| Distributable cash flow | \$ 55,365 | \$ 45,890 |

(4) Maintenance capital expenditures are capital expenditures made to replace partially or fully depreciated assets in order to maintain the existing operating capacity of our assets and to extend their useful lives. Maintenance capital expenditures include expenditures required to maintain equipment reliability, tankage and pipeline integrity, safety and to address environmental regulations.

As a master limited partnership, we distribute our available cash, which historically has exceeded our net income attributable to HEP because depreciation and amortization expense represents a non-cash charge against income. The result is a decline in partners' equity since our regular quarterly distributions have exceeded our quarterly net (5) income attributable to HEP. Additionally, if the assets contributed and acquired from HFC while we were a consolidated variable interest entity of HFC had been acquired from third parties, our acquisition cost in excess of HFC's basis in the transferred assets would have been recorded in our financial statements as increases to our properties and equipment and intangible assets at the time of acquisition instead of decreases to partners' equity.

Results of Operations—Three Months Ended March 31, 2016 Compared with Three Months Ended March 31, 2015

Summary

Net income attributable to Holly Energy Partners for the first quarter was \$42.8 million (\$0.52 per basic and diluted limited partner unit) compared to \$31.6 million (\$0.37 per basic and diluted limited partner unit) for the first quarter of 2015. The increase in earnings is primarily due to higher pipeline and terminal volumes and annual tariff increases, increased revenue from our UNEV products pipeline, our share of earnings from our 50% interest in Frontier Pipeline Company, and our refinery processing units acquired in the fourth quarter of 2015.

Our major shippers are obligated to make deficiency payments to us if they do not meet their minimum volume shipping obligations. Revenues for the three months ended March 31, 2016, include the recognition of \$6.6 million of prior shortfalls billed to shippers in 2015 compared to revenues for the three months ended March 31, 2015, which included the recognition of \$7.5 million of prior shortfalls billed to shippers in 2014. Additional shortfall billings of \$1.6 million associated with certain guaranteed shipping contracts were deferred during the three months ended March 31, 2016. Such deferred revenue will be recognized in earnings either as (a) payment for shipments in excess of guaranteed levels, if and to the extent the pipeline system will have the necessary capacity for shipments in excess of guaranteed levels, or (b) when shipping rights expire unused over the contractual make-up period.

Revenues

Revenues for the quarter were \$102.0 million, a \$12.3 million increase compared to the first quarter of 2015 due to the effect of higher pipeline volumes and annual tariff increases in addition to \$4.5 million increased revenue from the El Dorado refinery processing units. The volume increase resulted in overall pipeline volumes being up 5% compared to the three months ended March 31, 2015 largely due to increased volumes from pipelines servicing HFC's Navajo refinery and the UNEV pipeline.

Revenues from our refined product pipelines were \$39.9 million, an increase of \$3.7 million compared to the first quarter of 2015, mainly due to increased revenue from UNEV Pipeline of \$2.9 million in addition to increased volumes and annual tariff increases. Shipments averaged 210.8 mbpd compared to 186.9 mbpd for the first quarter of 2015 mainly due to increased volumes from pipelines servicing HFC's Navajo refinery and the UNEV pipeline.

- 30 -

Table of Contentsril 19,

Revenues from our intermediate pipelines were \$7.4 million, an increase of \$0.6 million, on shipments averaging 137.4 mbpd compared to 138.1 mbpd for the first quarter of 2015. Even though volumes decreased slightly, revenues increased due to annual tariff increases and an increase in deferred revenue realized.

Revenues from our crude pipelines were \$17.5 million, an increase of \$0.5 million, on shipments averaging 287.4 mbpd compared to 282.7 mbpd for the first quarter of 2015. Revenues increased mainly due to increased volumes and annual tariff increases.

Revenues from terminal, tankage and loading rack fees were \$32.7 million, an increase of \$3.0 million compared to the first quarter of 2015. Refined products terminalled in our facilities averaged 466.9 mbpd compared to 397.1 mbpd for the first quarter of 2015. The volume increase is mainly due to the inclusion of full quarter volumes from our El Dorado crude tanks acquired in the first quarter of 2015. Revenues reflect increased revenue from the El Dorado crude tanks as well as increased volumes and annual tariff increases.

Operations Expense

Operations (exclusive of depreciation and amortization) expense for the three months ended March 31, 2016, decreased by \$1.1 million compared to the three months ended March 31, 2015. The decrease is mainly due to lower environmental costs partially offset by operating expenses from the newly acquired El Dorado processing units.

Depreciation and Amortization

Depreciation and amortization for the three months ended March 31, 2016, increased by \$1.8 million compared to the three months ended March 31, 2015. The increase is principally due to increased depreciation from our newly acquired El Dorado operating units.

General and Administrative

General and administrative costs for the three months ended March 31, 2016, decreased by \$0.2 million compared to the three months ended March 31, 2015 mainly due to decreased professional fees and incentive compensation.

Equity in Earnings of Equity Method Investments

Our equity in earnings of the SLC Pipeline was \$1.0 million and \$0.7 million for the three months ended March 31, 2016 and 2015, respectively. Our equity in earnings of our 50% interest in Frontier Pipeline, purchased on August 31, 2015, was \$1.5 million for the quarter ended March 31, 2016. Our equity in earnings of our 50% interest in Osage Pipeline, purchased on February 22, 2016, was \$0.2 million for the three months ended March 31, 2016.

Interest Expense

Interest expense for the three months ended March 31, 2016, totaled \$10.5 million, an increase of \$1.8 million compared to the three months ended March 31, 2015. The increase is primarily due to a higher balance outstanding on the Credit Agreement. Our aggregate effective interest rates were 4.1% and 4.0% for the three months ended March 31, 2016 and 2015, respectively.

State Income Tax

We recorded a state income tax expense of \$95,000 and \$101,000 for the three months ended March 31, 2016 and 2015, respectively. All tax expense is solely attributable to the Texas margin tax.

LIQUIDITY AND CAPITAL RESOURCES

Overview

In March 2016, we amended our senior secured revolving credit facility (the "Credit Agreement") expiring in November 2018, increasing the size of the Credit Agreement from \$850 million to \$1.2 billion, which is available to fund capital

expenditures, investments, acquisitions, distribution payments and working capital and for general partnership purposes. It is also available to fund letters of credit up to a \$50 million sub-limit.

During the three months ended March 31, 2016, we received advances totaling \$522.0 million and repaid \$469.0 million, resulting in a net increase of \$53.0 million under the Credit Agreement and an outstanding balance of \$765.0 million at March 31, 2016. We have no letters of credit outstanding under the Credit Agreement at March 31, 2016, and the available capacity under the Credit Agreement is \$435.0 million at March 31, 2016.

If any particular lender under the Credit Agreement could not honor its commitment, we believe the unused capacity that would be available from the remaining lenders would be sufficient to meet our borrowing needs. Additionally, we review publicly available information on the lenders in order to monitor their financial stability and assess their ongoing ability to honor their

- 31 -

Table of Contentsril 19,

commitments under the Credit Agreement. We do not expect to experience any difficulty in the lenders' ability to honor their respective commitments, and if it were to become necessary, we believe there would be alternative lenders or options available.

Under our registration statement filed with the SEC using a "shelf" registration process, we currently have the authority to raise up to \$2.0 billion by offering securities, through one or more prospectus supplements that would describe, among other things, the specific amounts, prices and terms of any securities offered and how the proceeds would be used. Any proceeds from the sale of securities would be used for general business purposes, which may include, among other things, funding acquisitions of assets or businesses, working capital, capital expenditures, investments in subsidiaries, the retirement of existing debt and/or the repurchase of common units or other securities.

We believe our current cash balances, future internally generated funds and funds available under the Credit Agreement will provide sufficient resources to meet our working capital liquidity needs for the foreseeable future.

In February 2016, we paid regular quarterly cash distributions of \$0.565 on all units in an aggregate amount of \$45.0 million including \$10.9 million of incentive distribution payments to our general partner.

Contemporaneously with our UNEV Pipeline interest acquisition on July 12, 2012, HEP Logistics, our general partner, agreed to forego its right to incentive distributions of \$1.25 million per quarter over twelve consecutive quarterly periods following the close of the transaction and up to an additional four quarters if HFC's Woods Cross Refinery expansion did not attain certain thresholds. We expect HEP Logistics' waiver of its right to incentive distributions of \$1.25 million per quarter to end in the third quarter of 2016.

Cash and cash equivalents decreased by \$6.0 million during the three months ended March 31, 2016. The cash flows provided by operating activities of \$48.3 million were less than the cash flows used for financing activities of \$36.5 million and investing activities of \$17.8 million. Working capital increased by \$8.5 million to \$20.7 million at March 31, 2016, from \$12.2 million at December 31, 2015.

Cash Flows—Operating Activities

Cash flows from operating activities decreased by \$12.5 million from \$60.8 million for the three months ended March 31, 2015, to \$48.3 million for the three months ended March 31, 2016. This decrease is due principally to \$16.0 million of higher payments of affiliate accounts payable partially offset by higher cash receipts for services performed in the three months ended March 31, 2016, as compared to the prior year.

Cash Flows—Investing Activities

Cash flows used for investing activities were \$17.8 million for the three months ended March 31, 2016, compared to \$51.5 million for the three months ended March 31, 2015, an increase of \$33.7 million. During the three months ended March 31, 2016 and 2015, we invested \$17.9 million and \$24.2 million in additions to properties and equipment, respectively. We purchased the El Dorado crude tank assets for \$27.5 million in March 2015.

Cash Flows—Financing Activities

Cash flows used for financing activities were \$36.5 million for the three months ended March 31, 2016, compared to \$6.3 million for the three months ended March 31, 2015, an increase of \$30.2 million. During the three months ended March 31, 2016, we received \$522.0 million and repaid \$469.0 million in advances under the Credit Agreement. Additionally, we paid \$45.0 million in regular quarterly cash distributions to our general and limited partners, \$1.3 million to our noncontrolling interest and \$0.8 million for the purchase of common units for recipients of our incentive grants. We also paid \$39.5 million for the crude oil tanks located at HFC's Tulsa refinery acquired in March 2016, and we paid \$3.0 million in deferred financing charges to amend our credit agreement. During the three months ended March 31, 2015, we received \$153.5 million and repaid \$130.5 million in advances under the Credit Agreement. We paid \$40.9 million in regular quarterly cash distributions to our general and limited partners, distributed \$1.3 million

to our noncontrolling interest, and paid \$0.2 million for the purchase of common units for recipients of our incentive grants.

Capital Requirements

Our pipeline and terminalling operations are capital intensive, requiring investments to maintain, expand, upgrade or enhance existing operations and to meet environmental and operational regulations. Our capital requirements have consisted of, and are expected to continue to consist of, maintenance capital expenditures and expansion capital expenditures. "Maintenance capital expenditures" represent capital expenditures to replace partially or fully depreciated assets to maintain the operating capacity of existing assets. Maintenance capital expenditures include expenditures required to maintain equipment reliability, tankage and pipeline integrity, safety and to address environmental regulations. "Expansion capital expenditures" represent capital expenditures to expand the operating capacity of existing or new assets, whether through construction or acquisition. Expansion capital

- 32 -

Table of Contentsril 19,

expenditures include expenditures to acquire assets, to grow our business and to expand existing facilities, such as projects that increase throughput capacity on our pipelines and in our terminals. Repair and maintenance expenses associated with existing assets that are minor in nature and do not extend the useful life of existing assets are charged to operating expenses as incurred.

Each year the board of directors of HLS, our ultimate general partner, approves our annual capital budget, which specifies capital projects that our management is authorized to undertake. Additionally, at times when conditions warrant or as new opportunities arise, additional projects may be approved. The funds allocated for a particular capital project may be expended over a period in excess of a year, depending on the time required to complete the project. Therefore, our planned capital expenditures for a given year consist of expenditures approved for capital projects included in the current year's capital budget as well as, in certain cases, expenditures approved for capital projects in capital budgets for prior years. The 2016 capital budget is comprised of \$13 million for maintenance capital expenditures and \$57 million for expansion capital expenditures. We expect the majority of the expansion capital budget to be invested in refined product pipeline expansions, crude system enhancements, new storage tanks, and enhanced blending capabilities at our racks. In addition to our capital budget, we may spend funds periodically to perform capital upgrades or additions to our assets where a customer reimburses us for such costs. The upgrades or additions would generally benefit the customer over the remaining life of the related service agreements.

We are currently evaluating a potential dropdown from HFC of certain assets related to the initial phase of the expansion at HFC's Woods Cross refinery in the second half of 2016.

We expect that our currently planned sustaining and maintenance capital expenditures, as well as expenditures for acquisitions and capital development projects, will be funded with cash generated by operations, the sale of additional limited partner common units, the issuance of debt securities and advances under our Credit Agreement, or a combination thereof. With volatility and uncertainty at times in the credit and equity markets, there may be limits on our ability to issue new debt or equity financing. Additionally, due to pricing movements in the debt and equity markets, we may not be able to issue new debt and equity securities at acceptable pricing. Without additional capital beyond amounts available under the Credit Agreement, our ability to obtain funds for some of these capital projects may be limited.

Under the terms of the transaction to acquire HFC's 75% interest in UNEV, we issued to HFC a Class B unit comprising a noncontrolling equity interest in a wholly-owned subsidiary subject to redemption to the extent that HFC is entitled to a 50% interest in our share of annual UNEV earnings before interest, income taxes, depreciation, and amortization above \$30 million beginning July 1, 2016, and ending in June 2032, subject to certain limitations.

Credit Agreement

In March 2016, we amended our senior secured revolving credit facility (the "Credit Agreement") increasing the size of the Credit Agreement from \$850 million to \$1.2 billion. The Credit Agreement is available to fund capital expenditures, investments, acquisitions, distribution payments and working capital as well as for general partnership purposes. It is also available to fund letters of credit up to a \$50 million sub-limit.

Our obligations under the Credit Agreement are collateralized by substantially all of our assets. Indebtedness under the Credit Agreement involves recourse to HEP Logistics, our general partner, and is guaranteed by our material wholly-owned subsidiaries. Any recourse to HEP Logistics would be limited to the extent of its assets, which other than its investment in us, are not significant. We may prepay all loans at any time without penalty, except for payment of certain breakage and related costs.

The Credit Agreement imposes certain requirements on us with which we were in compliance with as of March 31, 2016, 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 into a merger or consolidation, or sell assets; and covenants that require maintenance of a specified EBITDA to interest expense ratio, total debt to EBITDA ratio and senior debt to EBITDA ratio. If an event of default exists under the Credit Agreement, the lenders will be able to accelerate the maturity of the debt and exercise other rights and remedies.

Senior Notes

We have \$300.0 million in aggregate principal amount outstanding of 6.5% senior notes (the “6.5% Senior Notes”) maturing March 2020. The 6.5% Senior Notes are unsecured and impose certain restrictive covenants, with which we were in compliance as of March 31, 2016, 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 6.5% 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 at varying premiums over face value under the 6.5% Senior Notes.

Table of Contentsril 19,

Indebtedness under the 6.5% Senior Notes involves recourse to HEP Logistics, our general partner, and is guaranteed by our wholly-owned subsidiaries. However, any recourse to HEP Logistics would be limited to the extent of its assets, which other than its investment in us, are not significant.

Long-term Debt

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

| | March 31, 2016 (In thousands) | December 31, 2015 |
|--|-------------------------------------|----------------------|
| Credit Agreement | \$765,000 | \$ 712,000 |
| 6.5% Senior Notes | | |
| Principal | 300,000 | 300,000 |
| Unamortized discount and debt issuance costs | (3,056) | (3,248) |
| | 296,944 | 296,752 |
| Total long-term debt | \$1,061,944 | \$ 1,008,752 |

See “Risk Management” for a discussion of our interest rate swaps.

Contractual Obligations

There were no significant changes to our long-term contractual obligations during this period.

Impact of Inflation

Inflation in the United States has been relatively moderate in recent years and did not have a material impact on our results of operations for the three months ended March 31, 2016 and 2015. Historically, the PPI has increased an average of 2.3% annually over the past five calendar years.

The substantial majority of our revenues are generated under long-term contracts that provide for increases in our rates and minimum revenue guarantees annually for increases in the PPI. Certain of these contracts have provisions that limit the level of annual PPI percentage rate increases. Although the recent PPI increase may not be indicative of additional increases to be realized in the future, a significant and prolonged period of high inflation could adversely affect our cash flows and results of operations if costs increase at a rate greater than the fees we charge our shippers.

Environmental Matters

Our operation of pipelines, terminals, and associated facilities in connection with the transportation and storage of refined products and crude oil is subject to stringent and complex federal, state, and local laws and regulations governing the discharge of materials into the environment, or otherwise relating to the protection of the environment. As with the industry generally, compliance with existing and anticipated laws and regulations increases our overall cost of business, including our capital costs to construct, maintain, and upgrade equipment and facilities. While these laws and regulations affect our maintenance capital expenditures and net income, we believe that they do not affect our competitive position given that the operations of our competitors are similarly affected. We believe our operations are in substantial compliance with applicable environmental laws and regulations. However, these laws and regulations, and the interpretation or enforcement thereof, are subject to frequent change by regulatory authorities, and we are unable to predict the ongoing cost to us of complying with these laws and regulations or the future impact of these laws and regulations on our operations. Violation of environmental laws, regulations, and permits can result in the imposition of significant administrative, civil and criminal penalties, injunctions, and construction bans or delays. A major discharge of hydrocarbons or hazardous substances into the environment could, to the extent the event is not insured, subject us to substantial expense, including both the cost to comply with applicable laws and regulations and

claims made by employees, neighboring landowners and other third parties for personal injury and property damage.

Under the Omnibus Agreement and certain transportation agreements and purchase agreements with HFC, HFC has agreed to indemnify us, subject to certain monetary and time limitations, for environmental noncompliance and remediation liabilities associated with certain assets transferred to us from HFC and occurring or existing prior to the date of such transfers.

We have an environmental agreement with Alon with respect to pre-closing environmental costs and liabilities relating to the pipelines and terminals acquired from Alon in 2005, under which Alon will indemnify us subject to certain monetary and time limitations.

- 34 -

Table of Contentsril 19,

There are environmental remediation projects in progress that relate to certain assets acquired from HFC. Certain of these projects were underway prior to our purchase and represent liabilities retained by HFC. At March 31, 2016, we have a net accrual of \$7.4 million that relates to environmental clean-up projects for which we have assumed liability or for which the indemnity provided for by HFC has expired or will expire. The remaining projects, including assessment and monitoring activities, are covered under the HFC environmental indemnification discussed above and represent liabilities of HFC.

CRITICAL ACCOUNTING POLICIES

Our discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities as of the date of the financial statements. Actual results may differ from these estimates under different assumptions or conditions. Our significant accounting policies are described in “Item 7. Management’s Discussion and Analysis of Financial Condition and Operations—Critical Accounting Policies” in our Annual Report on Form 10-K for the year ended December 31, 2015. Certain critical accounting policies that materially affect the amounts recorded in our consolidated financial statements include revenue recognition, assessing the possible impairment of certain long-lived assets and goodwill, and assessing contingent liabilities for probable losses. There have been no changes to these policies in 2016. We consider these policies to be the most critical to understanding the judgments that are involved and the uncertainties that could impact our results of operations, financial condition and cash flows.

New Accounting Pronouncements

Revenue Recognition

In May 2014, an accounting standard update was issued requiring revenue to be recognized when promised goods or services are transferred to customers in an amount that reflects the expected consideration for these goods or services. This standard has an effective date of January 1, 2018. We are evaluating the impact of this standard.

Consolidation

In February 2015, the FASB issued a standard that modifies existing consolidation guidance for reporting organizations that are required to evaluate whether they should consolidate certain legal entities. We adopted the new standard effective January 1, 2016. This standard had no impact on the entities we consolidate.

Financial Assets and Liabilities

In January 2016, an accounting standard update was issued requiring changes in the accounting and disclosures for financial instruments. This standard will become effective beginning with our 2018 reporting year. We are evaluating the impact of this standard.

Leases

In February 2016, an accounting standard update was issued requiring leases to be measured and recognized as a lease liability, with a corresponding right-of-use asset on the balance sheet. This standard has an effective date of January 1, 2019, and we are evaluating the impact of this standard.

Earnings Per Unit

In April 2015, an accounting standard update was issued requiring changes to the allocation of the earnings or losses of a transferred business for periods before the date of a dropdown of net assets accounted for as a common control transaction entirely to the general partner for purposes of calculating historical earnings per unit. We have adopted this standard as of January 1, 2016, as required. In connection with the dropdown of assets from HFC's Tulsa refinery on March 31, 2016, we reduced net income by \$0.2 million for the three months ending March 31, 2015. This reduction had no impact on the historical earnings per unit.

RISK MANAGEMENT

We use interest rate swaps (derivative instruments) to manage our exposure to interest rate risk.

As of March 31, 2016, we have two interest rate swaps with identical terms that hedge our exposure to the cash flow risk caused by the effects of LIBOR changes on \$150.0 million of Credit Agreement advances. The swaps effectively convert \$150.0 million

- 35 -

Table of Contentsril 19,

of our LIBOR based debt to fixed rate debt having an interest rate of 0.74% plus an applicable margin of 2.25% as of March 31, 2016, which equaled an effective interest rate of 2.99%. Both of these swap contracts mature in July 2017.

We review publicly available information on our counterparties in order to monitor their financial stability and assess their ongoing ability to honor their commitments under the interest rate swap contracts. These counterparties are large financial institutions. Furthermore, we have not experienced, nor do we expect to experience, any difficulty in the counterparties honoring their respective commitments.

The market risk inherent in our debt positions is the potential change arising from increases or decreases in interest rates as discussed below.

At March 31, 2016, we had an outstanding principal balance on our 6.5% Senior Notes of \$300 million. A change in interest rates generally would affect the fair value of the Senior Notes, but not our earnings or cash flows. At March 31, 2016, the fair value of our 6.5% Senior Notes was \$295.5 million. We estimate a hypothetical 10% change in the yield-to-maturity applicable to the 6.5% Senior Notes at March 31, 2016, would result in a change of approximately \$7.2 million in the fair value of the underlying notes.

For the variable rate Credit Agreement, changes in interest rates would affect cash flows, but not the fair value. At March 31, 2016, borrowings outstanding under the Credit Agreement were \$765.0 million. By means of our cash flow hedges, we have effectively converted the variable rate on \$150.0 million of outstanding borrowings to a fixed rate. For the remaining unhedged Credit Agreement borrowings of \$615.0 million, a hypothetical 10% change in interest rates applicable to the Credit Agreement would not materially affect our cash flows.

Our operations are subject to normal hazards of operations, including fire, explosion and weather-related perils. We maintain various insurance coverages, including business interruption insurance, subject to certain deductibles. We are not fully insured against certain risks because such risks are not fully insurable, coverage is unavailable, or premium costs, in our judgment, do not justify such expenditures.

We have a risk management oversight committee that is made up of members from our senior management. This committee monitors our risk environment and provides direction for activities to mitigate, to an acceptable level, identified risks that may adversely affect the achievement of our goals.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Market risk is the risk of loss arising from adverse changes in market rates and prices. See “Risk Management” under “Management’s Discussion and Analysis of Financial Condition and Results of Operations” for a discussion of market risk exposures that we have with respect to our long-term debt, which disclosure should be read in conjunction with the quantitative and qualitative disclosures about market risk contained in our Annual Report on Form 10-K for the fiscal year ended December 31, 2015. We utilize derivative instruments to hedge our interest rate exposure, as discussed under “Risk Management.”

Since we do not own products shipped on our pipelines or terminalled at our terminal facilities, we do not have direct market risks associated with commodity prices.

Item 4. Controls and Procedures

(a) Evaluation of disclosure controls and procedures

Our principal executive officer and principal financial officer have evaluated, as required by Rule 13a-15(b) under the Securities Exchange Act of 1934 (the “Exchange Act”), our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of the period covered by this quarterly report on Form 10-Q. Our disclosure controls and procedures are designed to provide reasonable assurance that the information we are required to disclose in the reports that we file or submit under the Exchange Act is accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required disclosure and is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission’s rules and forms. Based upon the evaluation, our principal executive officer and principal financial officer have concluded that our disclosure controls and procedures were effective as of March 31, 2016, at a reasonable level of assurance.

(b) Changes in internal control over financial reporting

There have been no changes in our internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) that occurred during our last fiscal quarter that have materially affected or are reasonably likely to materially affect our internal control over financial reporting.

- 36 -

Table of Contentsril 19,

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

We are a party to various legal and regulatory proceedings, which we believe will not have a material adverse impact on our financial condition, results of operations or cash flows.

Item 1A. Risk Factors

There have been no material changes in our risk factors as previously disclosed in Part 1, “Item 1A. Risk Factors” of our Annual Report on Form 10-K for the fiscal year ended December 31, 2015. In addition to the other information set forth in this quarterly report, you should consider carefully the factors discussed below and in our 2015 Form 10-K, which could materially affect our business, financial condition or future results. The risks described in this quarterly report and in our 2015 Form 10-K are not the only risks we face. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial may also materially and adversely affect our business, financial condition or future results.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

(c) Common Unit Repurchases Made in the Quarter

The following table discloses purchases of our common units made by us or on our behalf for the periods shown below:

| Period | Total Number of Units Purchased | Average Price Paid Per Unit | Total Number of Units Purchased as Part of Publicly Announced Plan or Program | Maximum Number of Units that May Yet be Purchased Under a Publicly Announced Plan or Program |
|---------------------------------|------------------------------------|--------------------------------|---|--|
| January 2016 | — | \$ — | — | \$ — |
| February 2016 | 13,965 | \$ 26.64 | — | \$ — |
| March 2016 | 13,300 | \$ 30.98 | — | \$ — |
| Total for January through March | 27,265 | | — | |

We have a Long-Term Incentive Plan for employees and non-employee directors who perform services for us. The units reported represent (a) purchases of 13,300 common units in the open market for delivery to the recipients of our restricted unit, phantom unit and performance unit awards under our Long-Term Incentive Plan at the time of grant or settlement, as applicable; and (b) the delivery of 13,965 common units (which units were previously issued to certain officers and other employees pursuant to restricted unit awards at the time of grant) by such officers and employees to provide funds for the payment of payroll and income taxes due at vesting in the case of officers and employees who did not elect to satisfy such taxes by other means.

Item 6. Exhibits

The Exhibit Index on page 40 of this Quarterly Report on Form 10-Q lists the exhibits that are filed or furnished, as applicable, as part of the Quarterly Report on Form 10-Q.

- 37 -

Table of Contentsril 19,

HOLLY ENERGY PARTNERS, L.P.

SIGNATURES

Pursuant to the requirements of the Securities and Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

HOLLY ENERGY PARTNERS, L.P.
(Registrant)

By: HEP LOGISTICS HOLDINGS, L.P.
its General Partner

By: HOLLY LOGISTIC SERVICES, L.L.C.
its General Partner

Date: May 4, 2016 /s/ Richard L. Voliva III
Richard L. Voliva III
Vice President and
Chief Financial Officer
(Principal Financial Officer)

Date: May 4, 2016 /s/ Kenneth P. Norwood
Kenneth P. Norwood
Vice President and Controller
(Principal Accounting Officer)

Table of Contentsril 19,

Exhibit Index

Exhibit
Number Description

- 3.1 First Amended and Restated Agreement of Limited Partnership of Holly Energy Partners, L.P. (incorporated by reference to Exhibit 3.1 of Registrant's Quarterly Report on Form 10-Q for its quarterly period ended June 30, 2004, File No. 1-32225).
- 3.2 Amendment No. 1 to the First Amended and Restated Agreement of Limited Partnership of Holly Energy Partners, L.P., dated February 28, 2005 (incorporated by reference to Exhibit 3.1 of Registrant's Form 8-K Current Report dated February 28, 2005, File No. 1-32225).
- 3.3 Amendment No. 2 to the First Amended and Restated Agreement of Limited Partnership of Holly Energy Partners, L.P., as amended, dated July 6, 2005 (incorporated by reference to Exhibit 3.1 of Registrant's Form 8-K Current Report dated July 6, 2005, File No. 1-32225).
- 3.4 Amendment No. 3 to First Amended and Restated Agreement of Limited Partnership of Holly Energy Partners, L.P., dated April 11, 2008 (incorporated by reference to Exhibit 4.1 of Registrant's Current Report on Form 8-K dated April 15, 2008, File No. 1-32225).
- 3.5 Amendment No. 4 to First Amended and Restated Agreement of Limited Partnership of Holly Energy Partners, L.P., dated January 16, 2013 (incorporated by reference to Exhibit 3.1 of Registrant's Current Report on Form 8-K dated January 16, 2013, File No. 1-32225).
- 3.6 Limited Partial Waiver of Incentive Distribution Rights under the First Amended and Restated Agreement of Limited Partnership of Holly Energy Partners, L.P., dated as of July 12, 2012 (incorporated by reference to Exhibit 3.1 of Registrant's Current Report on Form 8-K dated July 12, 2012, File No. 1-32225).
- 3.7 First Amended and Restated Agreement of Limited Partnership of Holly Energy Partners - Operating Company, L.P. (incorporated by reference to Exhibit 3.2 of Registrant's Quarterly Report on Form 10-Q for its quarterly period ended June 30, 2004, File No. 1-32225).
- 3.8 First Amended and Restated Agreement of Limited Partnership of HEP Logistics Holdings, L.P. (incorporated by reference to Exhibit 3.4 of Registrant's Quarterly Report on Form 10-Q for its quarterly period ended June 30, 2004, File No. 1-32225).
- 3.9 First Amended and Restated Limited Liability Company Agreement of Holly Logistic Services, L.L.C. (incorporated by reference to Exhibit 3.5 of Registrant's Quarterly Report on Form 10-Q for its quarterly period ended June 30, 2004, File No. 1-32225).
- 3.10 Amendment No. 1 to the First Amended and Restated Limited Liability Company Agreement of Holly Logistic Services, L.L.C., dated April 27, 2011 (incorporated by reference to Exhibit 3.1 of Registrant's Form 8-K Current Report dated May 3, 2011, File No. 1-32225).
- 3.11 First Amended and Restated Limited Liability Company Agreement of HEP Logistics GP, L.L.C. (incorporated by reference to Exhibit 3.6 of Registrant's Quarterly Report on Form 10-Q for its quarterly period ended June 30, 2004, File No. 1-32225).
- 4.1+ Fifth Supplemental Indenture dated March 22, 2016, among El Dorado Osage LLC, Holly Energy Partners, L.P., and Holly Energy Finance Corp., the other Guarantors and U.S. Bank National Association.
- 10.1 LLC Interest Purchase Agreement dated February 22, 2016 by and among HollyFrontier Refining & Marketing LLC, HollyFrontier Corporation, Holly Energy Partners - Operating, L.P. and Holly Energy Partners, L.P. (incorporated by reference to Exhibit 10.89 of Registrant's Annual Report on Form 10-K for its fiscal year ended December 31, 2015, File No. 1-32225).
- 10.2 Refined Products Terminal Transfer Agreement dated February 22, 2016 by and among HEP Refining Assets, L.P., Holly Energy Partners, L.P., El Paso Logistics LLC, HollyFrontier Corporation and Holly Energy Partners - Operating, L.P. (incorporated by reference to Exhibit 10.90 of Registrant's Annual Report on Form 10-K for its fiscal year ended December 31, 2015, File No. 1-32225).
- 10.3 Assignment and Assumption of Agreements dated February 22, 2016 by and among Holly Energy Partners - Operating, L.P., HEP Pipeline Assets, Limited Partnership, HEP Pipeline, L.L.C., HEP Refining Assets,

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L.P., HEP Refining, L.L.C., HEP Mountain Home, L.L.C. and HEP Woods Cross, L.L.C. (incorporated by reference to Exhibit 10.3 of Registrant's Current Report on Form 8-K dated February 22, 2016, File No. 001-32225).

10.4 Second Amended and Restated Pipelines and Terminals Agreement dated February 22, 2016 by and among HollyFrontier Refining & Marketing LLC, HollyFrontier Corporation, Holly Energy Partners - Operating, L.P. and Holly Energy Partners, L.P. (incorporated by reference to Exhibit 10.4 of Registrant's Current Report on Form 8-K dated February 22, 2016, File No. 001-32225).

10.5 Fourteenth Amended and Restated Omnibus Agreement dated February 22, 2016 by and among HollyFrontier Corporation, Holly Energy Partners, L.P. and certain of their respective subsidiaries (incorporated by reference to Exhibit 10.5 of Registrant's Current Report on Form 8-K dated February 22, 2016, File No. 001-32225).

10.6 Amended and Restated Master Throughput Agreement dated February 22, 2016 by and between HollyFrontier Refining & Marketing LLC and Holly Energy Partners - Operating, L.P. (incorporated by reference to Exhibit 10.6 of Registrant's Current Report on Form 8-K dated February 22, 2016, File No. 001-32225).

- 39 -

Table of Contentsril 19,

- Agreement and Amendment No. 5 to Second Amended and Restated Credit Agreement dated March 10, 2016, among Holly Energy Partners - Operating, L.P., certain of its affiliates acting as guarantors, Wells Fargo Bank, National Association, as administrative agent, an issuing bank and a lender, and certain other lenders party thereto (incorporated by reference to Exhibit 10.1 of Registrant's Form 8-K dated March 11, 2016, File No. 1-32225).
- 10.7
- 31.1+ Certification of Chief Executive Officer under Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2+ Certification of Chief Financial Officer under Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1++ Certification of Chief Executive Officer under Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2++ Certification of Chief Financial Officer under Section 906 of the Sarbanes-Oxley Act of 2002.

The following financial information from Holly Energy Partners, L.P.'s Quarterly Report on Form 10-Q for the quarter ended March 31, 2016, formatted in XBRL (Extensible Business Reporting Language):

- 101** (i) Consolidated Balance Sheets, (ii) Consolidated Statements of Income, (iii) Consolidated Statements of Comprehensive Income, (iv) Consolidated Statements of Cash Flows, (v) Consolidated Statement of Partners' Equity, and (vi) Notes to Consolidated Financial Statements.

+ Filed herewith.

++Furnished herewith.

** Filed electronically herewith.