

Sprague Resources LP
Form 10-Q
November 27, 2013
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2013

or

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

For the transition period _____ to _____

Commission file number: 001-36137

Sprague Resources LP

(Exact name of registrant as specified in its charter)

Delaware
(State of incorporation)

45-2637964
(I.R.S. Employer

Identification No.)

Two International Drive

Suite 200

Portsmouth, New Hampshire
(Address of principal executive offices)

03801
(Zip Code)

Registrant's telephone number, including area code: (800) 225-1560

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

Indicated 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 Regulations S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

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

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

As of November 27, 2013, the registrant had approximately 10,078,637 common units and approximately 10,071,970 subordinated units outstanding.

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Table of Contents**PART I - FINANCIAL INFORMATION****Item 1. Financial Statements****Sprague Resources LP****Balance Sheets**

	September 30, 2013 (Unaudited)	December 31, 2012
Assets		
Current assets:		
Cash	\$ 800	\$ 800
Total assets	\$ 800	\$ 800
Liabilities and partners equity		
Total liabilities	\$	\$
Partners equity:		
Organizational limited partner	990	990
General partner	10	10
Accumulated deficit	(200)	(200)
Total partners equity	800	800
Total liabilities and partners equity	\$ 800	\$ 800

The accompanying notes are an integral part of these financial statements.

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Sprague Resources LP

Notes to Unaudited Financial Statements

1. Nature of Operations

Sprague Resources LP (the Partnership) is a Delaware limited partnership formed on June 23, 2011 to engage in any lawful activity for which limited partnerships may be organized under the Delaware Revised Limited Partnership Act including, but not limited to, actions to form a limited liability company and/or acquire assets owned by Sprague Operating Resources LLC, a Delaware limited liability company and the Partnership's operating company (the Predecessor and OLLC), an entity engaged in the sale of energy products, as well as materials handling operations.

In connection with the completion on October 30, 2013 of the initial public offering (the IPO) of limited partner interests of the Partnership, Axel Johnson Inc. (the Parent) contributed to Sprague Resources Holdings LLC (Sprague Holdings) all of the ownership interests in the Predecessor. The Predecessor distributed to a wholly owned subsidiary of Sprague Holdings certain assets and liabilities, including among others, 100% of the equity investment in 9047-1137 Quebec Inc. (Kildair) and accounts receivable and cash in an aggregate amount equal to the net proceeds of the IPO. Sprague Holdings then contributed all of the ownership interests in the Predecessor to the Partnership. All of the assets and liabilities of the Predecessor contributed to the Partnership by Sprague Holdings were recorded at the Parent's historical cost as the foregoing transactions are among entities under common control.

2. Basis of Presentation

The financial statements included herein reflect all normal and recurring adjustments which, in the opinion of management, are necessary for a fair presentation of the Partnership's financial position at September 30, 2013 and December 31, 2012.

The financial statements were prepared in accordance with the requirements of the Securities and Exchange Commission (SEC) for interim financial information. As permitted under those rules, certain notes or other financial information that are normally required by U.S. generally accepted accounting principles (GAAP) to be included in annual financial statements have been condensed or omitted from these interim financial statements. These interim financial statements, therefore, should be read in conjunction with the consolidated financial statements and related notes of the Partnership included in the prospectus of Sprague Resources dated October 24, 2013, as filed with the SEC on October 28, 2013 (the Prospectus).

3. Subsequent Events

On October 30, 2013, in connection with the closing of the IPO, 8,500,000 of the Partnership's common units, representing a 42.2% limited partner interest in the Partnership, were sold at an initial public offering price of \$18.00 per unit. Total proceeds of the sale of the common units were \$153.0 million, before underwriting discounts and commissions, the structuring fee and estimated offering expenses. After the IPO, the Parent owns 1,571,970 common units and 10,071,970 subordinated units, representing an aggregate 57.8% limited partner interest in the Partnership.

Contribution, Conveyance and Assumption Agreement

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On October 30, 2013, in connection with the closing of IPO, the Parent, Sprague Holdings, the Partnership, Sprague Resources GP LLC, a Delaware limited liability company and the general partner of the Partnership (the General Partner), Sprague Massachusetts Properties LLC, a Delaware limited liability company and a wholly owned subsidiary of Sprague Holdings (Sprague Massachusetts), Sprague International Properties LLC, a Delaware limited liability company and a wholly owned subsidiary of Sprague Holdings (Sprague International), Sprague Canadian Properties LLC, a Delaware limited liability company and a wholly owned subsidiary of Sprague Holdings (Sprague Canadian) and the OLLC entered into a contribution, conveyance and assumption agreement (the Contribution Agreement). Pursuant to the Contribution Agreement, among other things, Sprague Holdings conveyed all of the ownership interests in the Predecessor to the Partnership (through the OLLC), in exchange for (a) 1,571,970 common units, representing a 7.8% limited partner interest in the Partnership, (b) 10,071,970 subordinated units, representing a 50% limited partner interest in the Partnership, (c) all of the equity interests in the Partnership classified as incentive distribution rights under the amended and restated agreement of limited partnership of the Partnership and (d) the right to receive the deferred issuance and distribution (as defined in the Contribution Agreement).

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Sprague Resources LP

Notes to Unaudited Financial Statements

Omnibus Agreement

On October 30, 2013, in connection with the closing of the IPO, the Partnership, the Parent, Sprague Holdings and the General Partner, entered into an omnibus agreement (the Omnibus Agreement). The Omnibus Agreement addresses the agreement of the Parent to offer to the Partnership and to cause the Parent's controlled affiliates to offer to the Partnership opportunities to acquire certain businesses and assets and the obligation of Sprague Holdings to indemnify the Partnership for certain liabilities. Pursuant to the Omnibus Agreement, the Parent agreed to continue to provide credit support to the Partnership, consistent with past practice, through December 31, 2016, if and to the extent such services are necessary and reasonable, and the Partnership agreed to use its commercially reasonable efforts to reduce, and eventually eliminate, the need for trade credit support from the Parent. The Omnibus Agreement may be terminated (other than with respect to the indemnification provisions) by any party to the Omnibus Agreement in the event that the Parent, directly or indirectly, owns less than 50% of the voting equity power of the General Partner.

Services Agreement

On October 30, 2013, in connection with the closing of the IPO, the Partnership, the General Partner, Sprague Holdings and Sprague Energy Solutions, Inc., a Delaware corporation and a wholly owned subsidiary of the Predecessor (Sprague Solutions), entered into an operational services agreement (the Services Agreement). Pursuant to the Services Agreement, the General Partner will provide certain general and administrative and operational services to the Partnership and Sprague Holdings, and the Partnership and Sprague Holdings will reimburse the General Partner for all costs and expenses incurred in connection with providing such services to the Partnership and Sprague Holdings. The Services Agreement does not limit the amount that may be reimbursed or paid by the Partnership to the General Partner. The initial term of the Services Agreement will expire on October 30, 2018. The Services Agreement will automatically renew at the end of the initial term for successive one-year terms until terminated in accordance with the terms thereof. The Services Agreement does not limit the ability of the officers and employees of the General Partner to provide services to other affiliates of Sprague Holdings or unaffiliated third parties.

Terminal Operating Agreement

On October 30, 2013, in connection with the closing of the IPO, Sprague Massachusetts and the OLLC entered into an exclusive terminal operating agreement (the Terminal Operating Agreement) with respect to the terminal in New Bedford, Massachusetts owned by Sprague Massachusetts. Pursuant to the Terminal Operating Agreement, the OLLC has the exclusive use and operation of, and retains title to all of the refined products stored at, the New Bedford terminal owned by Sprague Massachusetts in exchange for a monthly fee to Sprague Massachusetts. The initial term of the Terminal Operating Agreement will expire on October 30, 2018. The Terminal Operating Agreement will terminate upon 60 days' written notice from Sprague Holdings or Sprague Massachusetts in the event that Sprague Holdings or Sprague Massachusetts determines that termination is necessary to facilitate the sale or development of the New Bedford terminal. The New Bedford terminal is subject to a purchase and sale agreement pursuant to which a third party may acquire the terminal from Sprague Massachusetts. Subject to certain conditions, such acquisition may be consummated on or before January 5, 2016. If such acquisition is consummated, the Terminal Operating Agreement will automatically terminate.

Long-Term Incentive Plan

The General Partner adopted the Sprague Resources LP 2013 Long-Term Incentive Plan (the LTIP) effective immediately prior to the effective date of the IPO, for the benefit of employees, consultants and directors of the General Partner and its affiliates, who provide services to the General Partner or an affiliate. The LTIP provides the Partnership with the flexibility to grant unit options, restricted units, phantom units, unit appreciation rights, cash awards, distribution equivalent rights, substitute awards, and other unit-based awards, or any combination of the foregoing.

The LTIP will initially limit the number of common units that may be delivered pursuant to vested awards to 800,000 common units. On January 1 of each calendar year occurring after the second anniversary of the effective date and prior to the expiration of the LTIP, the total number of common units reserved and available for issuance under the LTIP will increase by 200,000 common units.

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Sprague Resources LP

Notes to Unaudited Financial Statements

The LTIP will expire upon the earlier of (i) its termination by the board of directors of the General Partner, (ii) the date common units are no longer available under the LTIP for grants or (iii) the tenth anniversary of the date the LTIP was approved by the General Partner.

Underwriting Agreement

On October 24, 2013, the Partnership, the General Partner, the OLLC and Sprague Holdings (the Partnership Parties) entered into an underwriting agreement (the Underwriting Agreement) with the underwriters named therein (the Underwriters), providing for the offer and sale by the Partnership, and the purchase by the Underwriters, of 8,500,000 common units at a price to the public of \$18.00 per common unit (\$16.965 per common unit, net of underwriting discounts and before payment of a structuring fee).

The Underwriting Agreement contains customary representations, warranties and agreements of the parties, and customary conditions to closing, obligations to the parties and termination provisions. The Partnership Parties have agreed to indemnify the Underwriters against certain liabilities, including liabilities under the Securities Act of 1933, as amended, and to contribute to payments the Underwriters may be required to make because of any of those liabilities.

Table of Contents**Sprague Operating Resources LLC (Predecessor)****Consolidated Balance Sheets**

	September 30, 2013	December 31, 2012
	(Unaudited)	
	(in thousands)	
Assets		
Current assets:		
Cash and cash equivalents	\$ 3,313	\$ 3,691
Accounts receivable, net	191,223	251,246
Inventories	325,085	472,596
Fair value of derivative assets	40,308	30,852
Deferred income taxes	17,508	14,258
Other current assets	31,193	32,858
Total current assets	608,630	805,501
Property, plant and equipment, net	201,234	177,080
Intangibles and other assets, net	18,308	20,772
Goodwill	50,424	50,894
Total assets	\$ 878,596	\$ 1,054,247
Liabilities and member s equity		
Current liabilities:		
Accounts payable	\$ 137,892	\$ 196,776
Accrued liabilities	36,994	48,949
Fair value of derivative liabilities	50,786	49,953
Current portion of long-term debt	463,747	317,186
Current portion of capital leases	709	709
Total current liabilities	690,128	613,573
Commitments and contingencies (Note 9)		
Long-term debt	572	232,007
Long-term capital leases	5,091	5,717
Other liabilities	18,586	19,208
Deferred income taxes	42,201	42,536
Total liabilities	756,578	913,041
Member s equity:		
Member s equity	129,809	146,779
Accumulated other comprehensive loss, net of tax	(7,791)	(5,573)

Total member s equity	122,018	141,206
Total liabilities and member s equity	\$ 878,596	\$ 1,054,247

The accompanying notes are an integral part of these financial statements.

Table of Contents**Sprague Operating Resources LLC (Predecessor)****Unaudited Consolidated Statements of Operations**

	Three Months Ended September 30, 2013 2012 (in thousands)		Nine Months Ended September 30, 2013 2012 (in thousands)	
Net sales	\$ 940,275	\$ 703,693	\$ 3,407,048	\$ 2,741,299
Cost of products sold	914,574	690,489	3,282,438	2,658,266
Gross margin	25,701	13,204	124,610	83,033
Operating costs and expenses:				
Operating expenses	12,844	10,287	40,444	32,393
Selling, general and administrative	12,633	9,870	39,689	32,370
Depreciation and amortization	4,034	2,493	12,471	7,458
Total operating costs and expenses	29,511	22,650	92,604	72,221
Operating (loss) income	(3,810)	(9,446)	32,006	10,812
Loss on impairment of fixed assets				(529)
Other (expense) income	(215)	(134)	601	(134)
Interest income	261	130	521	438
Interest expense	(7,207)	(4,855)	(21,846)	(16,273)
(Loss) income before income taxes and equity in net income of foreign affiliate	(10,971)	(14,305)	11,282	(5,686)
Income tax benefit (provision)	4,560	6,908	(6,078)	3,203
(Loss) income before equity in net loss of foreign affiliate	(6,411)	(7,397)	5,204	(2,483)
Equity in net loss of foreign affiliate		(3,361)		(1,009)
Net (loss) income	\$ (6,411)	\$ (10,758)	\$ 5,204	\$ (3,492)

The accompanying notes are an integral part of these financial statements.

Table of Contents**Sprague Operating Resources LLC (Predecessor)****Unaudited Consolidated Statements of Comprehensive (Loss) Income**

	Three Months Ended September 30, 2013 2012 (in thousands)		Nine Months Ended September 30, 2013 2012 (in thousands)	
Net (loss) income	\$ (6,411)	\$ (10,758)	\$ 5,204	\$ (3,492)
Other comprehensive income (loss), net of tax:				
Unrealized (loss) on interest rate swaps				
Net loss arising in the period	(165)	(625)	(303)	(1,716)
Reclassification adjustment for losses realized in income as interest expense	1,292	1,010	3,806	3,099
Net change in unrealized loss on interest rate swaps	1,127	385	3,503	1,383
Tax effect	(452)	(155)	(1,408)	(556)
	675	230	2,095	827
Foreign currency translation adjustment	853	1,795	(1,812)	2,052
Unrealized gain (loss) on inter-entity long-term foreign currency transactions	1,313		(2,501)	
Other comprehensive income (loss)	2,841	2,025	(2,218)	2,879
Comprehensive (loss) income	\$ (3,570)	\$ (8,733)	\$ 2,986	\$ (613)

The accompanying notes are an integral part of these financial statements.

Table of Contents**Sprague Operating Resources LLC (Predecessor)****Unaudited Consolidated Statements of Cash Flows**

	Nine Months Ended September 30, 2013 2012 (in thousands)	
Cash flows from operating activities		
Net income (loss)	\$ 5,204	\$ (3,492)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	15,056	9,779
Gain on sale of assets	(10)	(25)
Gain on insurance recovery	(777)	