Energy Transfer Partners, L.P.
Form 10-Q
January 09, 2006
Table of Contents

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 November 30, 2005

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 1-11727

ENERGY TRANSFER PARTNERS, L.P.

(Exact name of registrant as specified in its charter)

Delaware	**73-1493906**
(state or other jurisdiction or	**(I.R.S. Employer**
incorporation or organization)	**Identification No.)**

2838 Woodside Street

Dallas, Texas 75204

(Address of principal executive

offices and zip code)

(214) 981-0700

(Registrant s telephone number, including area code)

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 x No ¨

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

Large accelerated filer ¨ Accelerated filer x Non-accelerated filer ¨

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

Yes ¨ No x

At January 7, 2006, the registrant had units outstanding as follows:

Energy Transfer Partners, L.P.	106,985,711	Common Units

Table of Contents

FORM 10-Q

INDEX TO FINANCIAL STATEMENTS

Energy Transfer Partners, L.P. and Subsidiaries

	Page
PART I FINANCIAL INFORMATION	
ITEM 1. Financial Statements (Unaudited)	
Condensed Consolidated Balance Sheets November 30, 2005 and August 31, 2005	1
Condensed Consolidated Statements of Operations Three Months Ended November 30, 2005 and 2004	3
Consolidated Statements of Comprehensive Income (Loss) Three Months Ended November 30, 2005 and 2004	4
Consolidated Statements of Partners Capital Three Months Ended November 30, 2005	5
Condensed Consolidated Statements of Cash Flows Three Months Ended November 30, 2005 and 2004	6
Notes to Condensed Consolidated Financial Statements	7
ITEM 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS	28
ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK	40
ITEM 4. CONTROLS AND PROCEDURES	42
PART II OTHER INFORMATION	
ITEM 6. EXHIBITS	42
SIGNATURES	

Table of Contents

Forward-Looking Statements

Certain matters discussed in this report, excluding historical information, as well as some statements by Energy Transfer Partners, L.P., (Energy Transfer Partners or the Partnership) in periodic press releases and some oral statements of Energy Transfer Partners officials during presentations about the Partnership, include certain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Statements using words such as anticipate, believe, intend, project, plan, continue estimate, forecast, may, will, or similar expressions help identify forward-looking statements. Although the Partnership believes such forward-looking statements are based on reasonable assumptions and current expectations and projections about future events, no assurance can be given that every objective will be reached.

Actual results may differ materially from any results projected, forecasted, estimated or expressed in forward-looking statements since many of the factors that determine these results are subject to uncertainties and risks, difficult to predict, and beyond management s control. For additional discussion of risks, uncertainties and assumptions, see the Partnership s Annual Report on Form 10-K as amended on Form 10-K/A for the fiscal year ended August 31, 2005 filed with the Securities and Exchange Commission on November 14, 2005 and December 12, 2005, respectively.

Definitions

The following is a list of certain acronyms and terms generally used in the energy industry and throughout this document:

/d	per day
Bbls	barrels
Btu	British thermal unit, an energy measurement
Mcf	thousand cubic feet
MMBtu	million British thermal unit
MMcf	million cubic feet
Bcf	billion cubic feet
NGL	natural gas liquid, such as propane, butane and natural gasoline
LIBOR	London Interbank Offered Rate
NYMEX	New York Mercantile Exchange
Reservoir	A porous and permeable underground formation containing a natural accumulation of producible natural gas and/or oil that is confined by impermeable rock or water barriers and is separate from other reservoirs.

Table of Contents

PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

ENERGY TRANSFER PARTNERS, L.P. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except unit data)

(unaudited)

	November 30, 2005	August 31, 2005
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 17,915	$ 24,914
Marketable securities	3,320	3,452
Accounts receivable, net of allowance for doubtful accounts	907,186	847,028
Accounts receivable from related companies	1,717	4,479
Inventories	582,015	302,893
Other current assets	274,031	275,254
Total current assets	1,786,184	1,458,020
PROPERTY, PLANT AND EQUIPMENT, net	2,525,297	2,440,565
INVESTMENT IN AFFILIATES	37,031	37,353
GOODWILL	324,911	324,019
INTANGIBLES AND OTHER ASSETS, net	147,925	166,949
Total assets	$ 4,821,348	$ 4,426,906

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

Table of Contents

ENERGY TRANSFER PARTNERS, L.P. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except unit data)

(unaudited)

	November 30, 2005	August 31, 2005
LIABILITIES AND PARTNERS CAPITAL		
CURRENT LIABILITIES:		
Working capital facility	$ 52,000	$ 17,026
Accounts payable	942,347	818,775
Accounts payable to related companies	418	1,073
Customer deposits	19,930	88,038
Price risk management liabilities	78,065	104,772
Accrued and other current liabilities	222,080	179,778
Income taxes payable	15,128	2,063
Deferred taxes	6,390	
Current maturities of long-term debt	39,402	39,349
Total current liabilities	1,375,760	1,250,874
LONG-TERM DEBT, less current maturities	1,785,865	1,675,705
LONG-TERM AFFILIATED PAYABLE	2,033	2,005
NONCURRENT DEFERRED TAXES	111,604	111,185
OTHER NONCURRENT LIABILITIES	39,206	43,801
MINORITY INTERESTS	1,972	17,144
	3,316,440	3,100,714
COMMITMENTS AND CONTINGENCIES		
PARTNERS CAPITAL:		
Common Unitholders (106,894,514 and 106,889,904 units authorized, issued and outstanding at November 30, 2005 and August 31, 2005, respectively)	1,408,450	1,362,125
Class C Unitholders (1,000,000 units authorized, issued and outstanding at November 30, 2005 and August 31, 2005)		
Class E Unitholders (8,853,832 units authorized, issued and outstanding at November 30, 2005 and August 31, 2005 held by subsidiary and reported as treasury units)		
General Partner	55,508	49,384
Accumulated other comprehensive income (loss)	40,950	(85,317)
Total partners capital	1,504,908	1,326,192
Total liabilities and partners capital	$ 4,821,348	$ 4,426,906

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

Table of Contents

ENERGY TRANSFER PARTNERS, L.P. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per unit and unit data)

(unaudited)

	Three Months Ended November 30,	
	2005	**2004**
REVENUES:		
Midstream and transportation and storage	$ 2,208,533	$ 693,686
Propane and other	208,087	170,512
Total revenues	2,416,620	864,198
COSTS AND EXPENSES:		
Cost of products sold, midstream and transportation and storage	1,959,368	621,914
Cost of products sold, propane and other	131,259	105,991
Operating expenses	102,671	60,200
Depreciation and amortization	26,913	19,661
Selling, general and administrative	24,799	10,723
Total costs and expenses	2,245,010	818,489
OPERATING INCOME	171,610	45,709
OTHER INCOME (EXPENSE):		
Interest expense	(28,393)	(17,331)
Equity in earnings (losses) of affiliates	(274)	36
Loss on disposal of assets	(128)	(91)
Interest income and other, net	959	134
INCOME FROM CONTINUING OPERATIONS BEFORE MINORITY INTERESTS AND INCOME TAX EXPENSE	143,774	28,457
Minority interests	(1,555)	(158)
INCOME FROM CONTINUING OPERATIONS BEFORE INCOME TAX EXPENSE	142,219	28,299
Income tax expense	22,411	1,032
INCOME FROM CONTINUING OPERATIONS	119,808	27,267
INCOME FROM DISCONTINUED OPERATIONS		3,343
NET INCOME	119,808	30,610
GENERAL PARTNER S INTEREST IN NET INCOME	20,483	6,089

LIMITED PARTNERS INTEREST IN NET INCOME	$ 99,325	$ 24,521
BASIC NET INCOME PER LIMITED PARTNER UNIT		
Limited Partners income from continuing operations	$ 0.76	$ 0.24
Limited Partners income from discontinued operations		0.03
NET INCOME PER LIMITED PARTNER UNIT	$ 0.76	$ 0.27
BASIC AVERAGE NUMBER OF UNITS OUTSTANDING	106,894,514	89,243,910
DILUTED NET INCOME PER LIMITED PARTNER UNIT		
Limited Partners income from continuing operations	$ 0.76	$ 0.24
Limited Partners income from discontinued operations		0.03
NET INCOME PER LIMITED PARTNER UNIT	$ 0.76	$ 0.27
DILUTED AVERAGE NUMBER OF UNITS OUTSTANDING	107,180,936	89,391,631

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

Table of Contents

ENERGY TRANSFER PARTNERS, L.P. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

(in thousands)

(unaudited)

	Three Months Ended November 30,	
	2005	2004
Net income	$ 119,808	$ 30,610
Other comprehensive income (loss) before tax:		
Reclassification adjustment for gains and losses on derivative instruments included in net income accounted for as hedges before taxes of $698	100,550	14,787
Change in value of derivative instruments accounted for as hedges before taxes of $185	26,731	(15,522)
Change in value of available-for-sale securities before tax benefit of $1	(132)	(590)
Income tax expense related to items of other comprehensive income	(882)	
Comprehensive income	$ 246,075	$ 29,285
Reconciliation of Accumulated Other Comprehensive Income		
Balance, beginning of period	$ (85,317)	$ 32
Current period reclassification to earnings	100,550	14,787
Current period change	25,717	(16,112)
Balance, end of period	$ 40,950	$ (1,293)

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

4

Table of Contents

ENERGY TRANSFER PARTNERS, L.P. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF PARTNERS CAPITAL

(in thousands, except unit data)

(unaudited)

	Number of Common Units	Common	Class C	Class E	General Partner	Accumulated Other Comprehensive Income (Loss)	Total
Balance, August 31, 2005	106,889,904	$ 1,362,125	$	$	$ 49,384	$ (85,317)	$ 1,326,192
Unit distribution		(53,447)			(14,359)		(67,806)
Issuance of restricted Common Units	4,610						
Net change in accumulated other comprehensive income per accompanying statement						126,267	126,267
Deferred compensation on restricted units and long-term incentive plan		447					447
Net income		99,325			20,483		119,808
Balance, November 30, 2005	106,894,514	$ 1,408,450	$	$	$ 55,508	$ 40,950	$ 1,504,908

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

Table of Contents

ENERGY TRANSFER PARTNERS, L.P. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

(unaudited)

	Three Months Ended November 30,	
	2005	**2004**
NET CASH FLOWS PROVIDED BY OPERATING ACTIVITIES:	$ 11,717	$ 56,655
CASH FLOWS FROM INVESTING ACTIVITIES:		
Cash paid for acquisitions, net of cash acquired	(27,856)	(67,267)
Working capital settlement on prior year acquisitions	19,653	
Capital expenditures	(87,069)	(43,382)
Proceeds from the sale of assets	541	1,275
Net cash used in investing activities	(94,731)	(109,374)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from borrowings	635,792	91,214
Principal payments on debt	(491,867)	(19,831)
Capital contribution from General Partner		51
Unit distributions	(67,806)	(41,024)
Other	(104)	(191)
Net cash provided by financing activities	76,015	30,219
DECREASE IN CASH AND CASH EQUIVALENTS	(6,999)	(22,500)
CASH AND CASH EQUIVALENTS, beginning of period	24,914	81,745
CASH AND CASH EQUIVALENTS, end of period	$ 17,915	$ 59,245

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

ENERGY TRANSFER PARTNERS, L.P. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Dollar amounts in thousands, except unit and per unit data)

(unaudited)

1. OPERATIONS AND ORGANIZATION:

The accompanying condensed consolidated balance sheet as of August 31, 2005, which has been derived from audited financial statements, and the unaudited interim financial statements and notes thereto of the Partnership have been prepared in accordance with accounting principles generally accepted in the United States of America for interim consolidated financial information and pursuant to the rules and regulations of the Securities and Exchange Commission. Accordingly, they do not include all the information and footnotes required by accounting principles generally accepted in the United States of America for complete consolidated financial statements, however, the company believes that the disclosures made are adequate to make the information not misleading. The results of operations for interim periods are not necessarily indicative of the results to be expected for a full year due to the seasonal nature of the Partnership s operations, maintenance activities and the impact of forward natural gas prices and differentials on certain derivative financial instruments that are accounted for using mark-to-market accounting.

In the opinion of management, all adjustments (all of which are normal and recurring) have been made that are necessary to fairly state the consolidated financial position of Energy Transfer Partners and subsidiaries as of November 30, 2005 and the results of operations and cash flows for the three-month periods ended November 30, 2005 and 2004, respectively. The unaudited interim consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto of Energy Transfer Partners presented in the Partnership s Annual Report on Form 10-K for the fiscal year ended August 31, 2005, as amended on Form 10-K/A as filed with the Securities and Exchange Commission on November 14, 2005, and December 12, 2005, respectively.

Certain prior period amounts have been reclassified to conform to the condensed financial statements of the 2005 presentation. These reclassifications have no impact on net income or total partners capital. Prior periods have also been adjusted to reflect the sale of certain assets in the midstream segment as discontinued operations. See Note 2 for additional information.

Business Operations

In order to simplify the obligations of Energy Transfer Partners under the laws of several jurisdictions in which it conducts business, the Partnership s activities are conducted through two wholly-owned subsidiary operating partnerships, La Grange Acquisition, L.P. which conducts business under the assumed name of Energy Transfer Company (ETC OLP), a Texas limited partnership which is engaged in midstream and transportation and storage natural gas operations, and Heritage Operating L.P. (HOLP), a Delaware limited partnership, which is engaged in retail and wholesale propane operations (collectively the Operating Partnerships). The Partnership, the Operating Partnerships, and their other subsidiaries are collectively referred to in this report as Energy Transfer or the Partnership .

2. DISCONTINUED OPERATIONS:

In April 2005, the Partnership sold its assets in Oklahoma, referred to as the Elk City System, for $191,606 in cash and recorded a gain during fiscal year 2005 of $142,469, net of income taxes, on the sale. The sale of the Elk City System was accounted for as discontinued operations. Therefore, in accordance with Statement of Financial Accounting Standards, No. 144, *Accounting for the Impairment of Disposal of Long-lived Assets*, the Partnership has reported results of operations from these assets as discontinued operations for all periods presented on the condensed consolidated statements of operations as follows:

	Three Months Ended November 30, 2005	Three Months Ended November 30, 2004
Revenues	$	$ 43,464
Cost and expenses		(40,121)
Income from discontinued operations	$	$ 3,343

Table of Contents

3. USE OF ESTIMATES:

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. The natural gas industry conducts its business by processing actual transactions at the end of the month following the month of delivery. Consequently, the most current month s financial results for the midstream and transportation and storage segments are estimated using volume estimates and market prices. Any difference between estimated results and actual results are recognized in the following month s financial statements. Management believes that the operating results estimated for the three months ended November 30, 2005 represents the actual results in all material respects.

Some of the other more significant estimates made by management include, but are not limited to, allowances for doubtful accounts, the fair value of derivative instruments, useful lives for depreciation and amortization, purchase accounting allocations and subsequent realizability of intangible assets, settlement dates for purposes of estimating asset retirement obligations, litigation reserves, and general business and medical self-insurance reserves. Actual results could differ from those estimates.

4. ACCOUNTS RECEIVABLE:

ETC OLP s midstream and transportation and storage operations deal with counterparties that are typically either investment grade or are otherwise secured with a letter of credit or other forms of security (corporate guaranty or prepayment). Management reviews midstream and transportation and storage accounts receivable balances each week. Credit limits are assigned and monitored for all counterparties of the midstream and transportation and storage operations. Management believes that the occurrence of bad debt in the midstream and transportation and storage segments is not significant; therefore, an allowance for doubtful accounts for the midstream and transportation and storage segments was not deemed necessary at November 30, 2005 or August 31, 2005. Bad debt expense related to these receivables is recognized at the time an account is deemed uncollectible. There was no bad debt expense recognized for the three months ended November 30, 2005 and 2004 in the midstream and transportation and storage segments.

ETC OLP enters into netting arrangements with counterparties of derivative contracts to mitigate credit risk. Transactions are confirmed with the counterparty and the net amount is settled when due. Amounts outstanding under these netting arrangements are presented on a net basis in the condensed consolidated balance sheets.

HOLP grants credit to its customers for the purchase of propane and propane-related products. Included in accounts receivable are trade accounts receivable arising from HOLP s retail and wholesale propane operations. Accounts receivable for retail and wholesale propane operations are recorded as amounts billed to customers less an allowance for doubtful accounts. The allowance for doubtful accounts for the retail and wholesale propane segments is based on management s assessment of the realizability of customer accounts. Management considers the overall creditworthiness of the Partnership s customers, historical trends in collectability, and any specific disputes in determining the amount of allowance for doubtful accounts. Bad debt expense related to these receivables is recognized at the time an account is deemed uncollectible. Bad debt expense, net of recoveries of $186 and $168 was recognized for the three months ended November 30, 2005 and 2004, respectively.

Accounts receivable consisted of the following:

	November 30, 2005	August 31, 2005
Accounts receivable - midstream and transportation and storage	$ 813,676	$ 782,090
Accounts receivable - propane	97,526	69,014
Less allowance for doubtful accounts	(4,016)	(4,076)
Total, net	$ 907,186	$ 847,028

5. INVENTORIES:

ETC OLP s inventories consist principally of natural gas held in storage which is valued at the lower of cost or market utilizing the weighted average cost method. Propane inventories are also valued at the lower of cost or market. The cost of propane inventories is determined using weighted-average cost of propane delivered to the customer service locations, and includes storage fees and inbound freight costs, while the cost of appliances, parts, and fittings is determined by the first-in, first-out method. Inventories consisted of the following:

	November 30, 2005	August 31, 2005
Natural gas, propane and other NGLs	$ 568,176	$ 288,657
Appliances, parts and fittings and other	13,839	14,236
Total inventories	$ 582,015	$ 302,893

6. CUSTOMER DEPOSITS:

Included in customer deposits as of August 31, 2005 was $51,400 related to a prepayment made by a customer for natural gas that was physically delivered during the three months ended November 30, 2005.

Table of Contents

7. INCOME PER LIMITED PARTNER UNIT:

Basic net income per limited partner unit is computed in accordance with EITF Issue No. 03-6 *(* EITF 03-6 *) Participating Securities and the Two-Class method under FASB Statement No. 128,* by dividing limited partners interest in net income by the weighted average number of Common Units outstanding. In periods when the Partnership s aggregate net income exceeds the aggregate distributions, EITF 03-6 requires the Partnership to present earnings per unit as if all of the earnings for the periods were distributed (see table below). Diluted net income per limited partner unit is computed by dividing limited partners interest in net income, after considering the General Partner s interest, by the weighted average number of Common Units outstanding and the weighted average number of restricted units (Unit Grants) granted under the 2004 Unit Plan and predecessor plan. A reconciliation of net income and weighted average units used in computing basic and diluted earnings per unit is as follows (in thousands, except unit and per unit data):

	Three Months Ended November 30,	
	2005	**2004**
Net income	$ 119,808	$ 30,610
Adjustments:		
General Partner s incentive distributions	(18,087)	(5,477)
General Partner s equity ownership	(2,396)	(612)
Limited Partner s interest in net income	$ 99,325	$ 24,521
Additional earnings allocation to General Partner (a)	(18,300)	
Net income available to limited partners (a)	$ 81,025	$ 24,521
Weighted average limited partner units basic	106,894,514	89,243,910
Limited Partners basic income per unit from continuing operations (a)	$ 0.76	$ 0.24
Limited Partners basic income per unit from discontinued operations (a)		0.03
Basic net income per limited partner unit: (a)	$ 0.76	$ 0.27
Weighted average limited partner units	106,894,514	89,243,910
Dilutive effect of Incentive units	286,422	147,721
Weighted average limited partner units, assuming dilutive effect of incentive units	107,180,936	89,391,631
Limited Partners diluted income per unit from continuing operations	$ 0.76	$ 0.24
Limited Partners diluted income per unit from discontinued operations		0.03
Diluted net income per limited partner unit	$ 0.76	$ 0.27

(a) Basic and diluted net income per limited partner unit has been presented to reflect the application of EITF 03-6. The Partnership s net income for partners capital purposes is allocated to the General Partner and Limited Partners in accordance with their respective partnership percentages, after giving effect to any priority income allocations for incentive distributions, if any, to the Partnership s General Partner, the holders of the incentive distribution rights pursuant to the Partnership Agreement, which are declared and paid following the close of each quarter. For purposes of computing basic and diluted net income per limited partner unit, in periods, on a year to date basis, when the Partnership s aggregate net income exceeds the aggregate distributions for such year to date periods, an increased amount of net

income is allocated to the General Partner for the additional pro forma priority income attributable to the application of EITF 03-6. The General Partner is entitled to receive incentive distributions if the amount the Partnership distributes with respect to any quarter exceeds levels specified in the Partnership Agreement.

8. UNIT BASED COMPENSATION PLANS

On September 1, 2005, the Partnership adopted the modified prospective provisions of Statement of Financial Accounting Standards No. 123 (revised 2004) *Accounting for Stock-based Compensation* (SFAS 123R). Prior to the adoption of SFAS 123R, the Partnership followed the fair value recognition provisions of SFAS 123. SFAS 123R requires that grant-date fair value of stock options and other equity-based compensation is recognized based on the risk-free interest rate used, the expected life of the grants under each of the plans and the expected distributions on each of the units granted. The Partnership assumed a weighted average risk-free interest rate of 2.86% for the three months ended November 30, 2005, in estimating the present value of the future cash flows of the distributions during the vesting period on the measurement date of each grant. The weighted average fair value at the grant date of the awards outstanding for the three months ended November 30, 2005 was $17.48. Annual average cash distributions at the grant date were estimated to be $1.29 for the three months ended November 30, 2005. The expected life of each grant is assumed to be the minimum vesting period under certain performance criteria of each grant. The Partnership recognized deferred compensation expense of $447 and $402 for the three months ended November 30, 2005 and 2004, respectively, related to unit based compensation plans. Adoption of SFAS 123R did not have a material effect on the Partnership s income from continuing operations.

Table of Contents

2004 Unit Plan

Employee Grants. The Compensation Committee, in its discretion, may from time to time grant awards to any employee, upon such terms and conditions as it may determine appropriate and in accordance with specific general guidelines as defined by the Plan. As of November 30, 2005, 263,533 awards to employees were outstanding under the 2004 Unit Plan and 2,067 were forfeited. These awards will vest at a rate of one-third over the next three years based upon the achievement of certain performance criteria. The issuance of Common Units pursuant to the 2004 Unit Plan is intended to serve as a means of incentive compensation, therefore, no consideration will be payable by the plan participants upon vesting and issuance of the Common Units. On December 20, 2005, the Compensation Committee modified the terms of the grants awarded during fiscal year 2005, by issuing 88,183 Common Units for the grants which vested September 1, 2005, forfeiting 800 grants and granting 168,200 additional awards. Total units outstanding under the 2004 Unit Plan for employees as of December 20, 2005 were 342,750.

Director Grants. Each director who is not also (i) a shareholder or a direct or indirect employee of any parent, or (ii) a direct or indirect employee of Energy Transfer Partners, L.L.C., the Partnership, or a subsidiary (Director Participant), who is elected or appointed to the Board for the first time shall automatically receive, on the date of his or her election or appointment, an award of up to 2,000 Units (the Initial Director s Grant). Each Director Participant who is in office on September 1st shall automatically receive an award of Units equal to $15,000 divided by the fair market value of Common Units on such date (Annual Director s Grant). On September 1, 2005, 3,000 Director Grants vested and Common Units were issued under the predecessor plan. As of November 30, 2005, Initial Director s Grants and annual Director s Grants totaling 22,954 units were outstanding under the 2004 Unit Plan and the predecessor plan. On December 20, 2005, an additional 3,744 units were vested and/or forfeited bringing the outstanding total units awarded to current and former directors under the 2004 Unit Plan and predecessor plan to 19,210.

Long-Term Incentive Grants. The Compensation Committee may, from time to time, grant awards under the Plan to any executive officer or any employee it may designate as a participant in accordance with general guidelines under the Plan. As of November 30, 2005, there have been no Long-Term Incentive Grants made under the Plan.

9. ACQUISITIONS:

In January 2005, the Partnership acquired the controlling interests in HPL Consolidation LP (HPL) from American Electric Power Corporation (AEP) for approximately $825,000 subject to working capital adjustments. In addition the Partnership acquired working inventory of natural gas stored in the Bammel storage facilities and financed it through a short-term borrowing from an affiliate, which was repaid in full in April 2005. Under the terms of the transaction, the Partnership acquired all but a 2% limited partner interest in HPL. On November 10, 2005, the Partnership acquired the remaining 2% limited partnership interests in HPL for $16,560 in cash. The purchase price was allocated to PP&E and the minority interest liability associated with the 2% limited partner interests was eliminated. As a result, HPL became a wholly-owned subsidiary of ETC OLP. The Partnership also reached a settlement agreement with AEP in November 2005 related to certain inventory and working capital matters associated with the acquisition. The terms of the agreement were not material in relation to the Partnership s financial position or results of operations.

The unaudited pro forma consolidated results of operations for the three months ended November 30, 2004 are presented as if the acquisition of the controlling interests in HPL had occurred at the beginning of the period presented. The proforma consolidated net income and earnings per unit include the income from discontinued operations as presented on the condensed consolidated income statement for the three months ended November 30, 2004. The results do not necessarily reflect the results that would have been obtained if the acquisition had actually occurred on the dates indicated or results that may be expected in the future.

	Three Months Ended November 30, 2004
Revenues	$ 1,747,267
Net income	$ 1,688,627
Basic earnings per Limited Partner Unit	$ 0.29
Diluted earnings per Limited Partner Unit	$ 0.29

Table of Contents

10. WORKING CAPITAL FACILITY AND LONG-TERM DEBT:

On November 23, 2005, the Partnership filed a registered exchange offer to exchange newly issued 5.65% Senior Notes due 2012 (the 2012 Notes) that will be registered under the Securities Act of 1933 (the New Notes), for a like amount of outstanding 5.65% Senior Notes due 2012, which have not been registered under the Securities Act (the Old Notes). The sole purpose of the exchange offer is to fulfill the obligations of the Partnership under the registration rights agreement entered into in connection with the sale by the Partnership of the Old Notes on July 29, 2005. The 2012 Notes issued pursuant to the exchange will have substantially identical terms to the Old Notes. The 2012 Notes initially will be fully and unconditionally guaranteed by ETC OLP and all of the direct and indirect wholly-owned subsidiaries of ETC OLP guarantees the Partnership s obligations under its revolving credit facility. The exchange offer has not yet been completed.

As of November 30, 2005 the Partnership had an $800,000 unsecured Revolving Credit Facility available through January 10, 2010. Amounts borrowed under the Revolving Credit Facility bear interest at a rate based on either a Eurodollar rate or a prime rate. The weighted average interest rate was 5.346% for the amount outstanding as of November 30, 2005. The outstanding amount on the Revolving Credit Facility as of November 30, 2005 was $313,339 which includes $3,339 under the Swingline option. The Partnership also had outstanding letters of credit of $9,960 under the Revolving Credit Facility. Total amount available under the Credit Agreement as of November 30, 2005 was $476,701. On December 13, 2005, the Partnership closed on a new $900,000 five-year revolving credit facility. The new credit facility replaces the Partnership s $800,000 credit facility and extends the maturity date to December 10, 2010. The Revolving Credit Facility will be fully and unconditionally guaranteed by ETC OLP and all of the direct and indirect wholly-owned subsidiaries of ETC OLP guarantee the Partnership s obligations. The Revolving Credit Facility is unsecured and has equal rights to holders of the Partnership s other current and future unsecured debt.

A $75,000 Senior Revolving Working Capital Facility is available through December 31, 2006. Amounts borrowed under this Working Capital Facility bear interest at a rate based on either a Eurodollar rate or a prime rate. The weighted average interest rate was 5.801% for the amount outstanding at November 30, 2005. The maximum commitment fee payable on the unused portion of the facility is 0.50%. HOLP must reduce the principal amount of working capital borrowings to $10,000 for a period of not less than 30 consecutive days at least one time during each fiscal year. All receivables, contracts, equipment, inventory, general intangibles, cash concentration accounts of HOLP, and the capital stock of HOLP s subsidiaries secure the Senior Revolving Working Capital Facility. As of November 30, 2005, the Senior Revolving Working Capital Facility had a balance outstanding of $56,320, of which $52,000 was short-term. There were outstanding Letters of Credit for the Senior Revolving Working Credit of $6,052 at November 30, 2005. Effective September 1, 2005, HOLP entered into the Second Amendment to the Third Amended and Restated Credit Agreement. The amendment in its entirety states as follows: In no event shall the Letter of Credit Exposure exceed $15,000 at any time . All of the remaining terms, provisions and conditions of the existing Credit Agreement continue in full force and effect as within the March 31, 2004 Third Amended and Restated Credit Amendment. Letter of Credit exposure plus the Working Capital Loan cannot exceed the $75,000 maximum Working Capital Facility.

A $75,000 Senior Revolving Acquisition Facility is available through December 31, 2006. Amounts borrowed under the Acquisition Credit Facility bear interest at a rate based on either a Eurodollar rate or a prime rate. The maximum commitment fee payable on the unused portion of the facility is 0.50%. All receivables, contracts, equipment, inventory, general intangibles, cash concentration accounts of HOLP, and the capital stock of HOLP s subsidiaries secure the Senior Revolving Acquisition Facility. The weighted average interest rate was 5.720% for the outstanding balance of $49,500 at November 30, 2005.

11. COMMITMENTS, CONTINGENCIES, AND ENVIRONMENTAL LIABILITIES:

Commitments

The Partnership has forward commodity contracts, which will be settled by physical delivery. Short-term contracts, which expire in less than one year, require delivery of up to 449,831 MMBtu/d. Long-term contracts total require delivery of up to 263,202 MMBtu/d and extend through July 2018.

The Partnership, in the normal course of business, purchases, processes, and sells natural gas pursuant to long-term contracts and enters into long term transportation and storage agreements. Such contracts contain terms that are customary in the industry. The Partnership believes that such terms are commercially reasonable and will not have a material adverse effect on the Partnership s financial position or results of operations. The Partnership has also entered into several propane purchase and supply commitments with varying terms as to quantities and prices, which expire at various dates through March 2006.

Litigation

The Partnership s operating partnerships, ETC OLP and HOLP, may, from time to time, be involved in litigation and claims arising out of their respective operations in the normal course of business. Management is not aware of any material legal or governmental proceedings against ETC OLP or contemplated to be brought against ETC OLP, under the various environmental protection statutes to which it is subject. Propane is a flammable, combustible gas. Serious personal injury and significant property damage can arise in connection with its storage, transportation or use. In the ordinary course of business, HOLP is sometimes threatened with or named as a defendant in various lawsuits seeking actual and punitive damages for product liability, personal injury and property damage. The Partnership maintains liability insurance with insurers in amounts and with coverages and deductibles management believes are reasonable and prudent, and which are generally accepted in the industry. However, there can be no assurance that the levels of insurance protection currently in effect will continue to be available at reasonable prices or that such levels will remain adequate to protect the Partnership and its Operating Partnerships from material expenses related to product liability, personal injury or property damage in the future. Although any litigation is inherently uncertain, based on past experience, the information currently available and the availability of insurance coverage, we do not believe that pending or threatened litigation matters will have a material adverse effect on our financial condition or results of operations.

At the time of the HPL acquisition, the HPL Entities, their parent companies and AEP, were engaged in ongoing litigation with Bank of America (B of A) that related to AEP s acquisition of HPL in the Enron bankruptcy and B of A s financing of cushion gas stored in the Bammel Storage facility (Cushion Gas). This litigation is referred to as the Cushion Gas Litigation . Under the terms of the Purchase and Sale Agreement and the related Cushion Gas Litigation Agreement, AEP and its subsidiaries that were the sellers of the HPL Entities retained control of the Cushion Gas Litigation and have agreed to indemnify ETC OLP and the HPL Entities for any damages arising from the Cushion Gas Litigation and the loss of use of the Cushion Gas, up to a maximum of the amount paid by ETC OLP for the HPL Entities and the working gas inventory. The Cushion Gas Litigation Agreement terminates upon final resolution of the Cushion Gas Litigation. In addition, under the terms of the Purchase and Sale Agreement, AEP retained control of additional matters relating to ongoing litigation and environmental remediation and agreed to bear the costs of or indemnify ETC OLP and the HPL Entities for the costs related to such matters.

The Partnership or its subsidiaries is a party to various legal proceedings and/or regulatory proceedings incidental to its business. Certain claims, suits and complaints arising in the ordinary course of business have been filed or are pending against the Partnership. In the opinion of management, all such matters are either covered by insurance, are without merit or involve amounts which, if resolved unfavorably, would not have a significant effect on the financial position or results of operations of the Partnership. Once management determines that information pertaining to a legal proceeding indicates that it is probable that a liability has been incurred, an accrual is established equal to management s estimate of the likely exposure. For matters that are covered by insurance, the Partnership accrues the related deductible. As of November 30, 2005 and August 31, 2005, an accrual of $2,842 and $1,120, respectively was recorded as accrued and other current liabilities on the Partnership s condensed consolidated balance sheet.

Environmental

The Partnership s operations are subject to extensive federal, state and local environmental laws and regulations that require expenditures for remediation at operating facilities and waste disposal sites. Although the Partnership believes its operations are in substantial compliance with

applicable environmental laws and regulations, risks of additional costs and liabilities are inherent in the natural gas pipeline and processing business, and there can be no assurance that significant costs and liabilities will not be incurred. Moreover, it is possible that other developments, such as increasingly stringent environmental laws, regulations and enforcement policies thereunder, and claims for damages to property or persons resulting from the operations could result in substantial costs and liabilities. Accordingly, the Partnership has adopted policies, practices, and procedures in the areas of pollution control, product safety, occupational health, and the handling, storage, use, and disposal of hazardous materials to prevent

material environmental or other damage, and to limit the financial liability, which could result from such events. However, some risk of environmental or other damage is inherent in the natural gas pipeline and processing business, as it is with other entities engaged in similar businesses.

Environmental exposures and liabilities are difficult to assess and estimate due to unknown factors such as the magnitude of possible contamination, the timing and extent of remediation, the determination of the Partnership s liability in proportion to other parties, improvements in cleanup technologies and the extent to which environmental laws and regulations may change in the future. Although environmental costs may have a significant impact on the results of operations for any single period, the Partnership believes that such costs will not have a material adverse effect on its financial position. As of November 30, 2005 and August 31, 2005, an accrual on an undiscounted basis of $1,998 and $2,036, respectively, was recorded in the Partnership s condensed consolidated balance sheet to cover material environmental liabilities including certain matters assumed in connection with the HPL acquisition. A receivable of $394 and $404 was recorded in the Partnership s balance sheets as of November 30, 2005 and August 31, 2005, respectively.

12. PRICE RISK MANAGEMENT ASSETS AND LIABILITIES:

Accounting for Derivative Instruments and Hedging Activities

The Partnership applies Statement of Financial Accounting Standards No. 133, *Accounting for Derivative Instruments and Hedging Activities* (SFAS 133) as amended. This statement requires that all derivatives be recognized in the balance sheet as either an asset or liability measured at fair value. Special accounting for qualifying hedges allows a derivative s gains and losses to offset related results on the hedged item in the statement of operations and requires that a company must formally document, designate and assess the effectiveness of transactions that receive hedge accounting treatment.

The Partnership has established a formal risk management policy in which derivative financial instruments are employed in connection with an underlying asset, liability and/or anticipated transaction. At inception of a hedge, the Partnership formally documents the relationship between the hedging instrument and the hedged item, the risk management objectives, and the methods used for assessing and testing effectiveness. The Partnership also assesses, both at the inception of the hedge and on a quarterly basis, whether the derivatives that are used in its hedging transactions are highly effective in offsetting changes in cash flows. Furthermore, management meets on a weekly basis to assess the creditworthiness of the derivative counterparties to manage against the risk of default. If the Partnership determines that a derivative is no longer highly effective as a hedge, it discontinues hedge accounting prospectively by including changes in the fair value of the derivative in current earnings.

Non-trading Activities

The Partnership utilizes various exchange-traded and over-the-counter commodity financial instrument contracts to limit its exposure to margin fluctuations in natural gas and NGL prices. These contracts consist primarily of futures and swaps. The Partnership designates various futures and certain associated basis contracts as cash flow hedging instruments in accordance with SFAS 133. All derivatives are recognized in the condensed consolidated balance sheet as price risk management assets or liabilities and are measured at fair value. For those instruments that do not qualify for hedge accounting, the change in market value is recorded as cost of products sold in the condensed consolidated statement of operations. The fair value of price risk management assets and liabilities that are designated and documented as cash flow hedges and determined to be effective are recorded through other comprehensive income. The effective portion of the hedge gain or loss is initially reported as a component of other comprehensive income and when the physical transaction settles, any gain or loss previously recorded in other comprehensive income (loss) on the derivative is recognized in cost of products sold in the condensed consolidated statement of operations. The

ineffective portion of the gain or loss is reported immediately in cost of products sold in the condensed consolidated statement of operations. As of November 30, 2005 and August 31, 2005, these hedging instruments had a net fair value of $(11,632) and $(101,325), respectively, which was recorded as other current assets, intangibles and other assets, price risk management liabilities and other noncurrent liabilities on the condensed consolidated balance sheet. The Partnership reclassified into earnings losses of $101,314 and $14,787 for the three months ended November 30, 2005 and 2004, respectively, related to the commodity financial instruments that were previously reported in accumulated other comprehensive income (loss). The amount of hedge ineffectiveness recognized in income by the Partnership was a loss of $18,322 and $15,342 for the three months ending November 30, 2005 and 2004, respectively. The Partnership expects gains of $1,649 to be reclassified into earnings over the next twelve

Table of Contents

months related to income currently reported in accumulated other comprehensive income. The majority of the Partnership s derivatives are expected to settle within the next two years.

In the course of normal operations, the Partnership routinely enters into contracts such as forward physical contracts for the purchase and sale of natural gas, propane, and other NGLs that qualify for and are designated as a normal purchase and sales contracts. Such contracts are exempted from the fair value accounting requirements of SFAS 133 and are accounted for using accrual accounting. In connection with the HPL acquisition, the Partnership acquired certain physical forward contracts that contain embedded options. These contracts have not been designated as normal purchases and sales contracts, and therefore, are marked to market in addition to the financial options that offset them. The Black Scholes valuation model was used to estimate the value of these embedded derivatives.

Trading Activities

During the fourth quarter of fiscal year 2005, the Partnership adopted a new risk management policy that provides for our marketing operations to execute limited strategies. Certain strategies are considered trading for accounting purposes and are executed with the use of a combination of financial instruments including, but not limited to, futures and basis trades. The Partnership accounts for its trading activities under the provisions of EITF Issue No. 02-3, *Accounting for Contracts Involved in Energy Trading and Risk Management Activities* (EITF 02-3), which requires revenue and costs related to energy trading contracts to be presented on a net basis in the income statement. The derivative contracts that are entered into for trading purposes, subject to limits, are recognized on the condensed consolidated balance sheet at fair value, and changes in the fair value of these derivative instruments are recognized in midstream and transportation and storage revenue in the condensed consolidated statement of operations. Revenues associated with trading activities for the three months ended November 30, 2005 were $52,579, including unrealized gains of $6,414.

The market prices used to value the financial derivative transactions reflect management s estimates considering various factors including closing exchange and over-the-counter quotations.

The following table details the outstanding derivatives as of November 30, 2005 and August 31, 2005, respectively:

November 30, 2005:	**Commodity**	**Notional Volume MMBTU**	**Maturity**	**Fair Value**
Mark to Market Derivatives				
(Non-Trading)				
Basis Swaps IFERC/NYMEX	Gas	(72,311,707)	2005-2007	$ 59,478
Swing Swaps IFERC	Gas	(31,722,376)	2005-2006	$ (3,869)
Fixed Swaps/Futures	Gas	1,862,500	2005-2007	$ (1,649)
Options	Gas	(642,000)	2005-2008	$ 69,976
Forward Physical Contracts	Gas	(17,250,000)	2005-2008	$ (69,976)
(Trading)				
Basis Swaps IFERC/NYMEX	Gas	(101,635,000)	2005-2007	$ 43,158
Swing Swaps IFERC	Gas	(22,149,999)	2005-2008	$ 3,972
Fixed Swaps/Futures	Gas	(655,000)	2005-2006	$ 3,175
Forward Physical Contracts	Gas	(237,200)	2005-2006	$ 3,260
Cash Flow Hedging Derivatives				

(Non-Trading)				
Fixed Swaps/Futures	Gas	(51,992,500)	2005-2007	$ (52,140)
Fixed Index Swaps	Gas	4,360,000	2005-2006	$ 22,479
Basis Swaps IFERC/NYMEX	Gas	(8,407,500)	2005-2006	$ 18,029

August 31, 2005:

Mark to Market Derivatives				
(Non-Trading)				
Basis Swaps IFERC/NYMEX	Gas	(34,196,114)	2005-2007	$ 646
Swing Swaps IFERC	Gas	(25,636,504)	2005-2006	(6,400)
Fixed Swaps/Futures	Gas	(1,960,000)	2005-2006	$ (7,423)

Table of Contents

August 31, 2005 (continued):	Commodity	Notional Volume MMBTU	Maturity	Fair Value
(Non-Trading)				
Options	Gas	(1,776,000)	2005-2008	$ 78,941
Forward Physical Contracts	Gas	(21,340,000)	2005-2008	$ (78,941)
(Trading)				
Basis Swaps IFERC/NYMEX	Gas	(55,772,500)	2005-2007	$ 49,833
Swing Swaps IFERC	Gas	(42,204,999)	2005-2008	$ (3,686)
Fixed Swaps/Futures	Gas	(150,000)	2005	$ 559
Forward Physical Contracts	Gas		2005	$ 441
Cash Flow Hedging Derivatives				
Fixed Swaps/Futures	Gas	(41,827,500)	2005-2007	$ (141,142)
Fixed Index Swaps	Gas	5,910,000	2005-2006	$ 36,455
Basis Swaps IFERC/NYMEX	Gas	(6,877,500)	2005-2006	$ 3,361

Estimates related to the Partnership s gas marketing activities are sensitive to uncertainty and volatility inherent in the energy commodities markets and actual results could differ from these estimates. The Partnership also attempts to maintain balanced positions in its non-trading activities to protect itself from the volatility in the energy commodities markets; however, net unbalanced positions can exist. Long-term physical contracts are tied to index prices. System gas, which is also tied to index prices, will provide the gas required by our long-term physical contracts. When third-party gas is required to supply long-term contracts, a hedge is put in place to protect the margin on the contract. Financial contracts, which are not tied to physical delivery, will be offset with financial contracts to balance the Partnership s positions. To the extent open commodity positions exist, fluctuating commodity prices can impact the Partnership s financial results and financial position, either favorably or unfavorably.

Interest Rate Risk

The Partnership is exposed to market risk for changes in interest rates related to the bank credit facilities of the Partnership. The Partnership manages a portion of its interest rate exposures by utilizing interest rate swaps and similar arrangements which allow the Partnership to effectively convert a portion of variable rate debt into fixed debt.

Forward starting interest swaps with a notional amount of $150,000 were entered into and outstanding as of November 30, 2005 and had a fair value of $3,562 which was recorded as unrealized losses in accumulated other

comprehensive income (loss) and a component of price risk management liabilities in the condensed consolidated balance sheet. Ineffectiveness related to the forward starting interest swaps during the three months ended November 30, 2005 was a gain of $771 which was recorded as a component of interest expense. The outstanding interest rate swaps as of November 30, 2005 were entered into in anticipation of a bond offering to occur in the third quarter of fiscal year 2006.

ETC OLP also had an interest rate swap with a notional amount of $75,000 that matured in October 2005. As of November 30, 2005 and August 31, 2005, the interest rate swap had a fair value of $0 and $151, respectively. Under the terms of the swap agreement, the Partnership paid a fixed rate of 2.76% and received three-month LIBOR with a quarterly settlement. The interest rate swap was not accounted for as a hedge but received mark to market accounting. Accordingly, changes in the fair value are recorded as a component of interest expense in the condensed consolidated statement of operations

The following represents gain (loss) on derivative activity for the periods presented:

	Three Months Ended November 30,	
	2005	**2004**
Unrealized gain (loss) recognized in revenues and cost of products sold related to Partnership s derivative activity	$ 55,231	$ (8,903)
Realized gain (loss) included in revenues and cost of products sold	$ (9,293)	$ 12,536
Unrealized gain on interest rate swap included in interest expense	$ 620	$ 502
Realized gain (loss) on interest rate swap included in interest expense	$ 143	$ (233)

13. QUARTERLY DISTRIBUTIONS OF AVAILABLE CASH:

On October 15, 2005, the Partnership paid a quarterly distribution of $0.50 per unit, or $2.00 per unit annually, to the Unitholders of record at the close of business on September 30, 2005. On December 5, 2005, the Partnership declared a cash distribution for the first quarter ended November 30, 2005 of $0.55 per unit, or $2.20 per unit annually, payable on January 13, 2006 to Unitholders of record at the close of business on January 4, 2006. In addition to these quarterly distributions, the General Partner, Energy Transfer Partners, GP, L.P. (ETP GP), received quarterly distributions for its general partner interest in the Partnership and incentive distributions to the extent the quarterly distribution exceeded $0.275 per unit. The total amount of distributions declared relating to the quarter ended November 30, 2005 on Common Units, the Class E, the General Partner interests and the Incentive Distribution Rights totaled $58,842, $3,121, $1,634, and $18,087, respectively. All such distributions were made from Available Cash from Operating Surplus.

14. INCOME TAXES:

Energy Transfer Partners, L.P. is a limited partnership. As a result, the Partnership s earnings or losses for federal and state income tax purposes are included in the tax returns of the individual partners. Net earnings for financial statement purposes may differ significantly from taxable income reportable to unitholders as a result of differences between the tax basis and financial reporting basis of assets and liabilities in addition to the taxable income allocation requirements under the Partnership Agreement.

Certain of the Partnership s subsidiaries are taxable corporations and follow the asset and liability method of accounting for income taxes in accordance with Statement of Financial Accounting Standards No. 109, *Accounting for Income Taxes* (SFAS 109). Under SFAS 109, deferred income taxes are recorded based upon differences between the financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the underlying assets are received and liabilities settled. During the three months ended November 30, 2005, a subsidiary treated as a taxable corporation accrued $19,000 in income tax expense due to higher taxable income recognized by this subsidiary. The higher taxable income was attributed to gains on financial derivative activity recognized by this subsidiary. The income tax provision was based on an estimated tax rate of 35% of this subsidiary s taxable income.

Table of Contents

15. RELATED PARTY TRANSACTIONS:

As of November 30, 2005 and August 31, 2005, accounts receivable from related companies was $1,717 and $4,479, respectively. Included in the receivable from related companies as of November 30, 2005 and August 31, 2005 was a net receivable of $0 and $2,098, respectively, due from ETP GP comprised of its 2% contribution due for the July 2005 private placement of 3,000,000 Common Units. Related party receivables due from various related companies related to receivables in the normal course of business as of November 30, 2005 and August 31, 2005 was $1,717 and $2,381, respectively. Total accounts payable to related companies of $418 and $1,073 as of November 30, 2005 and August 31, 2005, respectively, included $393 and $746, respectively, due to Energy Transfer Equity, L.P. (ETE) related to the Energy Transfer Transactions. Also included in the total accounts payable to related companies as of November 30, 2005 and August 31, 2005 is approximately $25 and $327, respectively, payable to unconsolidated companies for purchases of natural gas and operating expenses incurred in the normal course of business.

As of November 30, 2005 and August 31, 2005, the Partnership had a note payable of $2,033 and $2,062, respectively, related to its contribution in a cylinder exchange joint venture entered into July 2005 in which it owns a 50% interest. The note bears interest at an annual rate equal to the one month LIBOR rate plus 150 basis points, compounded monthly. The note is recorded as long-term affiliated payable on the Partnership s condensed consolidated balance sheets. Included in accounts receivable from related companies as of November 30, 2005 and August 31, 2005 is a receivable of $1,404 and $689, respectively, from this joint venture for administrative support services provided to and cash payments made on behalf of the joint venture by the Partnership.

The Partnership s natural gas midstream and transportation and storage operations secure compression services from various suppliers including Energy Transfer Technologies, Ltd. Energy Transfer Group, LLC is the general partner of Energy Transfer Technologies, Ltd. These entities are collectively referred to as the ETG Entities . The Partnership s Co-Chief Executive Officers have an indirect ownership in the ETG Entities. In addition, two of the General Partner s directors serve on the Board of Directors of the ETG Entities. The terms of each arrangement to provide compression services are, in the opinion of management, no less favorable than those available from other providers of compression services. For the three months ending November 30, 2005 and 2004, payments totaling $1,198 and $370, respectively, were made to the ETG Entities for compression services provided to and utilized in the Partnership s natural gas midstream and transportation and storage operations.

16. SUMMARIZED CONDENSED CONSOLIDATING FINANCIAL STATEMENTS:

The Partnership s Revolving Credit Facility and Senior Notes are fully and unconditionally guaranteed by ETC OLP and all of the direct and indirect wholly-owned subsidiaries of ETC OLP (the Subsidiary Guarantors). HOLP and its direct and indirect subsidiaries and Heritage Holdings, Inc. do not guarantee the Partnership s Revolving Credit Facility and Senior Notes. The Subsidiary Guarantors, jointly and severally guarantee, on an unsecured senior basis, the Partnership s obligations under the Partnership s Revolving Credit Facility and Senior Notes. Following are unaudited condensed consolidating financial information of the Partnership, the Subsidiary Guarantors, the Non-Guarantor Subsidiaries and the Partnership on a consolidated basis. The condensed consolidating financial information presented herein complies with Rule 3-10 of Regulation S-X, is prepared on the equity method, and does not contain related financial statement disclosures that would be required with a complete set of financial statements presented in conformity with accounting principles generally accepted in the United States of America.

ENERGY TRANSFER PARTNERS, L.P. AND SUBSIDIARIES

UNAUDITED CONDENSED CONSOLIDATING BALANCE SHEET

As of November 30, 2005

(In thousands)

	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated
ASSETS					
CURRENT ASSETS:					
Cash and cash equivalents	$ 1,153	$ 38	$ 16,724	$	$ 17,915
Marketable securities			3,320		3,320
Accounts receivable, net of allowance for doubtful accounts		813,676	93,510		907,186
Accounts receivable from related companies	203,422	11,458	2,592	(215,755)	1,717
Inventories		465,816	116,199		582,015
Other current assets	4,479	255,445	14,107		274,031
Total current assets	209,054	1,546,433	246,452	(215,755)	1,786,184
PROPERTY, PLANT AND EQUIPMENT, net	9	2,013,070	512,218		2,525,297
INVESTMENT IN AFFILIATES	2,914,967	32,300	141,141	(3,051,377)	37,031
GOODWILL		23,736	301,175		324,911
INTANGIBLES AND OTHER ASSETS, net	12,687	36,855	98,383		147,925
Total assets	$ 3,136,717	$ 3,652,394	$ 1,299,369	$ (3,267,132)	$ 4,821,348
LIABILITIES AND PARTNERS CAPITAL					
CURRENT LIABILITIES:					
Working capital facility	$	$	$ 52,000	$	$ 52,000
Accounts payable	747	843,537	98,063		942,347
Accounts payable to related companies	8,705	207,242	226	(215,755)	418
Other current liabilities	25,121	209,696	106,776		341,593
Current maturities of long-term debt			39,402		39,402
Total current liabilities	34,573	1,260,475	296,467	(215,755)	1,375,760
LONG-TERM DEBT, net of discount, less current maturities	1,460,826		325,039		1,785,865
LONG-TERM AFFILIATED PAYABLE			2,033		2,033
DEFERRED TAXES		52,245	59,359		111,604
OTHER NONCURRENT LIABILITIES		39,206			39,206
MINORITY INTERESTS			1,972		1,972
	1,495,399	1,351,926	684,870	(215,755)	3,316,440
COMMITMENTS AND CONTINGENCIES					
PARTNERS CAPITAL	1,641,318	2,300,468	614,499	(3,051,377)	1,504,908
Total liabilities and partners capital	$ 3,136,717	$ 3,652,394	$ 1,299,369	$ (3,267,132)	$ 4,821,348

ENERGY TRANSFER PARTNERS, L.P. AND SUBSIDIARIES

UNAUDITED CONDENSED CONSOLIDATING BALANCE SHEET

As of August 31, 2005

(In thousands)

	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated
ASSETS					
CURRENT ASSETS:					
Cash and cash equivalents	$ 3,810	$ 38	$ 21,066	$	$ 24,914
Marketable securities			3,452		3,452
Accounts receivable, net of allowance for doubtful accounts		782,090	64,938		847,028
Accounts receivable from related companies	99,833	12,515	1,858	(109,727)	4,479
Inventories		225,325	77,568		302,893
Other current assets	917	266,509	7,828		275,254
Total current assets	104,560	1,286,477	176,710	(109,727)	1,458,020
PROPERTY, PLANT AND EQUIPMENT, net	9	1,938,160	502,396		2,440,565
INVESTMENT IN AFFILIATES	2,718,945	32,601	144,283	(2,858,476)	37,353
GOODWILL		23,736	300,283		324,019
INTANGIBLES AND OTHER ASSETS, net	13,057	56,099	97,793		166,949
Total assets	$ 2,836,571	$ 3,337,073	$ 1,221,465	$ (2,968,203)	$ 4,426,906
LIABILITIES AND PARTNERS CAPITAL					
CURRENT LIABILITIES:					
Working capital facility	$	$	$ 17,026	$	$ 17,026
Accounts payable	2,181	764,590	52,004		818,775
Accounts payable to related companies	9,461	100,865	474	(109,727)	1,073
Other current liabilities	10,774	270,465	93,412		374,651
Current maturities of long-term debt			39,349		39,349
Total current liabilities	22,416	1,135,920	202,265	(109,727)	1,250,874
LONG-TERM DEBT, less current maturities	1,348,432		327,273		1,675,705
LONG-TERM AFFILIATED PAYABLE			2,005		2,005
DEFERRED TAXES		52,854	58,331		111,185
MINORITY INTERESTS		15,319	1,825		17,144
OTHER NONCURRENT LIABILITIES		43,801			43,801
	1,370,848	1,247,894	591,699	(109,727)	3,100,714
COMMITMENTS AND CONTINGENCIES					
PARTNERS CAPITAL	1,465,723	2,089,179	629,766	(2,858,476)	1,326,192
Total liabilities and partners capital	$ 2,836,571	$ 3,337,073	$ 1,221,465	$ (2,968,203)	$ 4,426,906

20

Table of Contents

ENERGY TRANSFER PARTNERS, L.P. AND SUBSIDIARIES

UNAUDITED CONDENSED CONSOLIDATING STATEMENT OF OPERATIONS

For the three months ended November 30, 2005

(In thousands)

	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated
REVENUES:					
Midstream and transportation and storage	$	$ 2,208,533	$	$	$ 2,208,533
Propane and other			208,087		208,087
Total revenue		2,208,533	208,087		2,416,620
COSTS AND EXPENSES:					
Cost of products sold		1,959,368	131,259		2,090,627
Operating expenses		53,677	48,994		102,671
Depreciation and amortization		13,419	13,494		26,913
Selling, general and administrative	2,820	18,787	3,192		24,799
Total costs and expenses	2,820	2,045,251	196,939		2,245,010
OPERATING INCOME (LOSS)	(2,820)	163,282	11,148		171,610
OTHER INCOME (EXPENSE):					
Interest expense	(20,604)	(2,320)	(7,730)	2,261	(28,393)
Equity in earnings (losses) of affiliates	141,321	(251)	(23)	(141,321)	(274)
Gain (loss) on disposal of assets		10	(138)		(128)
Other, net	1,911	1,402	(93)	(2,261)	959
INCOME FROM CONTINUING OPERATIONS BEFORE MINORITY INTERESTS AND INCOME TAX EXPENSE	119,808	162,123	3,164	(141,321)	143,774
Minority interests		(1,349)	(206)		(1,555)
INCOME FROM CONTINUING OPERATIONS BEFORE INCOME TAX EXPENSE	119,808	160,774	2,958	(141,321)	142,219
Income tax expense		19,005	3,406		22,411
NET INCOME (LOSS)	$ 119,808	$ 141,769	$ (448)	$ (141,321)	$ 119,808

21

Table of Contents

ENERGY TRANSFER PARTNERS, L.P. AND SUBSIDIARIES

UNAUDITED CONDENSED CONSOLIDATING STATEMENT OF OPERATIONS

For the three months ended November 30, 2004

(see Note 2)

(In thousands)

	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated
REVENUES:					
Midstream and transportation	$	$ 693,686	$	$	$ 693,686
Propane and other			170,512		170,512
Total revenue		693,686	170,512		864,198
COSTS AND EXPENSES:					
Cost of products sold		621,914	105,991		727,905
Operating expenses		16,093	44,107		60,200
Depreciation and amortization		6,336	13,325		19,661
Selling, general and administrative	1,114	6,578	3,031		10,723
Total costs and expenses	1,114	650,921	166,454		818,489
OPERATING INCOME (LOSS)	(1,114)	42,765	4,058		45,709
OTHER INCOME (EXPENSE):					
Interest expense	(961)	(9,703)	(7,628)	961	(17,331)
Equity in earnings of affiliates	32,664	14	22	(32,664)	36
Loss on disposal of assets		(17)	(74)		(91)
Other, net	22	1,195	(122)	(961)	134
INCOME (LOSS) FROM CONTINUING OPERATIONS BEFORE MINORITY INTERESTS AND INCOME TAX EXPENSE	30,611	34,254	(3,744)	(32,664)	28,457
Minority interests			(158)		(158)
INCOME FROM CONTINUING OPERATIONS BEFORE INCOME TAX EXPENSE	30,611	34,254	(3,902)	(32,664)	28,299
Income tax expense (benefit)		(57)	1,089		1,032
INCOME (LOSS) FROM CONTINUING OPERATIONS	30,611	34,311	(4,991)	(32,664)	27,267
INCOME FROM DISCONTINUED OPERATIONS		3,343			3,343