

SUNOCO INC
Form 10-Q
August 04, 2011
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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

June 30, 2011 For the quarterly period ended June 30, 2011

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 1-6841

SUNOCO, INC.

(Exact name of registrant as specified in its charter)

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Pennsylvania
(State or other jurisdiction of
incorporation or organization)

23-1743282
(I.R.S. Employer
Identification No.)

1818 Market Street, Suite 1500, Philadelphia, PA
(Address of principal executive offices)

19103
(Zip Code)

Registrant's telephone number, including area code: (215) 977-3000

(Former name, former address and former fiscal year, if changed since last report): **Not Applicable**

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 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.

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

At June 30, 2011, there were 121,139,215 shares of Common Stock, \$1 par value outstanding.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements (Unaudited)**SUNOCO, INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**

(Millions of Dollars and Shares, Except Per-Share Amounts)

	For the Six Months Ended June 30,	
	2011	2010
	(UNAUDITED)	
Revenues		
Sales and other operating revenue (including consumer excise taxes)	\$ 22,607	\$ 17,738
Interest income	12	1
Other income, net	42	39
	22,661	17,778
Costs and Expenses		
Cost of products sold and operating expenses	20,823	15,661
Consumer excise taxes	1,101	1,138
Selling, general and administrative expenses	315	313
Depreciation, depletion and amortization	224	236
Payroll, property and other taxes	61	58
Provision for asset write-downs and other matters (Note 3)	300	67
Interest cost and debt expense	82	79
Interest capitalized	(12)	(6)
	22,894	17,546
Income (loss) from continuing operations before income tax expense (benefit)	(233)	232
Income tax expense (benefit) (Note 4)	(82)	71
Income (loss) from continuing operations	(151)	161
Loss from discontinued operations, net of income taxes (Note 2)		(23)
Net income (loss)	(151)	138
Less: net income attributable to noncontrolling interests	75	56
Net income (loss) attributable to Sunoco, Inc. shareholders	\$ (226)	\$ 82
Earnings (loss) attributable to Sunoco, Inc. shareholders per share of common stock:		
Basic:		
Income (loss) from continuing operations	\$ (1.87)	\$ 0.88
Loss from discontinued operations		(0.19)
Net income (loss)	\$ (1.87)	\$ 0.69
Diluted:		

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Income (loss) from continuing operations	\$ (1.87)	\$ 0.88
Loss from discontinued operations		(0.19)
Net income (loss)	\$ (1.87)	\$ 0.69
Weighted-average number of shares outstanding (Note 5):		
Basic	121.0	119.7
Diluted	121.0	119.7
Cash dividends paid per share of common stock	\$ 0.30	\$ 0.30
(See Accompanying Notes)		

Table of Contents**SUNOCO, INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**

(Millions of Dollars and Shares, Except Per-Share Amounts)

	For the Three Months Ended June 30,	
	2011	2010
	(UNAUDITED)	
Revenues		
Sales and other operating revenue (including consumer excise taxes)	\$ 11,998	\$ 9,572
Interest income	8	1
Other income, net	17	13
	12,023	9,586
Costs and Expenses		
Cost of products sold and operating expenses	11,004	8,350
Consumer excise taxes	553	608
Selling, general and administrative expenses	170	167
Depreciation, depletion and amortization	112	122
Payroll, property and other taxes	24	24
Provision for asset write-downs and other matters (Note 3)	294	22
Interest cost and debt expense	39	40
Interest capitalized	(6)	(3)
	12,190	9,330
Income (loss) before income tax expense (benefit)	(167)	256
Income tax expense (benefit) (Note 4)	(96)	80
Net income (loss)	(71)	176
Less: net income attributable to noncontrolling interests	54	31
Net income (loss) attributable to Sunoco, Inc. shareholders	\$ (125)	\$ 145
Earnings (loss) attributable to Sunoco, Inc. shareholders per share of common stock:		
Basic	\$ (1.03)	\$ 1.20
Diluted	\$ (1.03)	\$ 1.20
Weighted-average number of shares outstanding (Note 5):		
Basic	121.1	120.6
Diluted	121.1	120.7
Cash dividends paid per share of common stock	\$ 0.15	\$ 0.15

(See Accompanying Notes)

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SUNOCO, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

(Millions of Dollars)

	At June 30, 2011 (UNAUDITED)	At December 31, 2010
Assets		
Cash and cash equivalents	\$ 1,476	\$ 1,485
Accounts and notes receivable, net	3,044	2,679
Inventories:		
Crude oil	383	98
Petroleum and chemical products	371	126
Coal and coke	114	83
Materials, supplies and other	102	97
Deferred income taxes	121	129
Assets held for sale (Note 3)	118	1,029
Total current assets	5,729	5,726
Investments and long term receivables	163	160
Note receivable from sale of Toledo refinery (Note 3)	200	
Properties, plants and equipment, cost	10,779	11,263
Less: accumulated depreciation, depletion and amortization	3,736	4,208
Properties, plants and equipment, net	7,043	7,055
Deferred charges and other assets	377	356
Total assets	\$ 13,512	\$ 13,297
Liabilities and Equity		
Accounts payable	\$ 4,164	\$ 3,912
Accrued liabilities (Note 6)	657	554
Short-term borrowings	115	115
Current portion of long-term debt	278	178
Taxes payable	240	170
Total current liabilities	5,454	4,929
Long-term debt	2,085	2,136
Retirement benefit liabilities (Note 7)	478	481
Deferred income taxes	1,314	1,390
Other deferred credits and liabilities (Note 6)	564	562
Commitments and contingent liabilities (Note 6)		
Total liabilities	9,895	9,498
Equity (Note 9)		
Sunoco, Inc. shareholders' equity	2,828	3,046
Noncontrolling interests	789	753

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Total equity		3,617		3,799
Total liabilities and equity		\$ 13,512		\$ 13,297

(See Accompanying Notes)

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(Millions of Dollars)

	For the Six Months Ended June 30,	
	2011	2010
	(UNAUDITED)	
Cash Flows from Operating Activities:		
Net income (loss)	\$ (151)	\$ 138
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Loss on divestment of discontinued polypropylene operations		169
Provision for asset write-downs and other matters	300	67
Depreciation, depletion and amortization	224	239
Deferred income tax benefit	(191)	(10)
Payments less than (in excess of) expense for retirement plans	5	(126)
Changes in working capital pertaining to operating activities:		
Accounts and notes receivable	(366)	(29)
Inventories	(591)	(319)
Accounts payable and accrued liabilities	362	447
Income tax refund receivable and taxes payable	71	389
Other	(20)	(9)
Net cash provided by (used in) operating activities	(357)	956
Cash Flows from Investing Activities:		
Capital expenditures	(328)	(341)
Acquisitions	(124)	
Proceeds from divestments:		
Discontinued polypropylene operations		348
Toledo refinery and related inventory	837	
Other divestments	8	18
Other	(9)	(2)
Net cash provided by investing activities	384	23
Cash Flows from Financing Activities:		
Net repayments of short-term borrowings		(282)
Net proceeds from issuance of long-term debt	297	802
Repayments of long-term debt	(243)	(462)
Net proceeds from sale of Sunoco Logistics Partners L.P. limited partnership units		145
Cash distributions to noncontrolling interests	(58)	(61)
Cash dividend payments	(36)	(36)
Other	4	
Net cash provided by (used in) financing activities	(36)	106
Net increase (decrease) in cash and cash equivalents	(9)	1,085
Cash and cash equivalents at beginning of period	1,485	377
Cash and cash equivalents at end of period	\$ 1,476	\$ 1,462

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(See Accompanying Notes)

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The accompanying condensed consolidated financial statements are presented in accordance with the requirements of Form 10-Q and U.S. generally accepted accounting principles for interim financial reporting. They do not include all disclosures normally made in financial statements contained in Form 10-K. In management's opinion, all adjustments necessary for a fair presentation of the results of operations, financial position and cash flows for the periods shown have been made. All such adjustments are of a normal recurring nature, except for the gain on divestment of the Toledo refinery and related inventory, the gain resulting from the reduction of crude oil and refined product inventories at the Toledo refinery prior to its sale, the gain on the remeasurement of the pipeline equity interest, the loss on the divestment of the polypropylene chemicals business and the provision for asset write-downs and other matters (Notes 2, 3 and 11). Results for the three and six months ended June 30, 2011 are not necessarily indicative of results for the full-year 2011.

2. Discontinued Polypropylene Operations.

On March 31, 2010, Sunoco completed the sale of the common stock of its polypropylene chemicals business to Braskem S.A. The assets sold as part of this transaction included the polypropylene manufacturing facilities in LaPorte, TX, Neal, WV, and Marcus Hook, PA, a propylene supply agreement and related inventory. Cash proceeds from this divestment of \$348 million were received in the second quarter of 2010. As a result of the sale of the polypropylene chemicals business, such operations have been classified as discontinued operations in the condensed consolidated statements of operations. Sunoco recognized a net loss of \$169 million (\$44 million after tax) related to the divestment which was reflected as a component of the loss from discontinued operations in the first quarter of 2010.

The following is a summary of the loss from discontinued operations which was recognized during the first quarter of 2010 (in millions of dollars):

Loss before income tax benefit	\$ (136)
Income tax benefit	(113)
Loss from discontinued operations*	\$ (23)

* Attributable to Sunoco, Inc. shareholders.

Sales and other operating revenue (including consumer excise taxes) from discontinued operations totaled \$313 million during the first quarter of 2010.

**3. Changes in Business and Other Matters.
Acquisitions**

In January 2011, SunCoke Energy acquired Harold Keene Coal Co., Inc. (HKCC), based in Honaker, VA, for \$52 million. The purchase price included a net cash payment of \$38 million and contingent consideration totaling \$14 million primarily related to the estimated fair value of contingent royalty payments to the seller if certain minimum production levels are met for a period of up to 20 years. The assets acquired, which are adjacent to SunCoke Energy's existing mining operations, include two active underground mines and one active surface and highwall mine currently producing between 250 and 300 thousand tons of coal annually. Proven and probable coal reserve estimates for this acquisition total approximately 21 million tons.

In May 2011, Sunoco Logistics Partners L.P. (the Partnership) obtained a controlling financial interest in Inland Corporation (Inland) through a series of transactions involving Sunoco and a third party. Sunoco exercised its rights to acquire additional ownership interests in Inland for \$56

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million, net of cash received, and the Partnership purchased additional ownership interests from a third party for \$30 million. The Partnership's total ownership interest in Inland increased to 84 percent after it purchased all of Sunoco's interests. As a result of these transactions, Inland became a consolidated subsidiary of Sunoco and, in connection therewith, Sunoco recognized a \$9 million gain (\$6 million after tax) from the remeasurement of its pre-acquisition equity interests in Inland to fair value upon consolidation. This gain is included in other income, net, in the condensed consolidated statements of operations.

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The following table summarizes the effects of Sunoco's acquisitions during the first half of 2011 on its consolidated financial position (including the consolidation of Inland and the recognition of the gain from the remeasurement of the pre-acquisition equity interests) (in millions of dollars):

	HKCC	Inland*	Total
Increase in:			
Current assets	\$ 8	\$ 3	\$ 11
Properties, plants and equipment	64	175	239
Deferred charges and other assets**	8		8
Current liabilities	(4)	(5)	(9)
Deferred income taxes	(23)	(59)	(82)
Other deferred credits and liabilities	(1)	(1)	(2)
Sunoco, Inc. shareholders' equity		(6)	(6)
Noncontrolling interests		(18)	(18)
Decrease in:			
Investments and long-term receivables		(3)	(3)
	52	86	138
Contingent consideration	(14)		(14)
Cash paid for acquisitions, net of cash received	\$ 38	\$ 86	\$ 124

* Based on preliminary valuation results.

** Includes \$6 million allocated to goodwill.

No pro forma information has been presented since the impact of these acquisitions was not material in relation to Sunoco's consolidated results of operations.

In June 2011, the Partnership signed a definitive agreement to purchase a refined products terminal located in East Boston, MA from ConocoPhillips for \$56 million plus the fair value of inventory. The terminal has a storage capacity of approximately 1.2 million barrels and is the sole service provider of Logan International Airport under a long term contract. The transaction is subject to customary closing conditions and is expected to close in the third quarter of 2011.

In August 2011, the Partnership acquired a crude oil purchasing and marketing business from Texon L.P. (Texon) for \$205 million plus the fair value of inventory. The purchase consists of a lease crude business and gathering assets in 16 states, primarily in the western United States. The current crude oil volume of the business is approximately 75 thousand barrels per day. The purchase was financed with a portion of the net proceeds from the Partnership's senior notes offering in July 2011 (see Note 12).

Divestments

On March 1, 2011, Sunoco completed the sale of its Toledo refinery and related crude and refined product inventories to a wholly owned subsidiary of PBF Holding Company LLC. The Company received \$1,037 million in net proceeds consisting of \$546 million in cash at closing, a \$200 million two-year note receivable, and a \$285 million note receivable and \$6 million in cash related to working capital adjustments subsequent to closing which were both paid in May 2011. In addition, the purchase agreement also includes a participation payment of up to \$125 million based on the future profitability of the refinery. Sunoco has not recorded any amount related to the contingent consideration in accordance with its accounting policy election on such amounts. In connection with this transaction, the Company recognized a \$6 million net pretax gain (\$1 million loss after tax) in the first half of 2011 which is included in other income, net, in the condensed consolidated statements of operations. This gain includes a pretax gain of \$535 million attributable to the sale of crude and refined product inventories. In addition, Sunoco reduced crude oil and refined product inventories at the Toledo refinery prior to the sale which resulted in LIFO inventory profits of \$42 million (\$26 million after tax) during the first quarter of 2011. The results of operations for the Toledo refinery have not been classified as discontinued operations due to Sunoco's continuing involvement with the Toledo refinery through a three-year agreement for the purchase of gasoline and distillate to supply Sunoco retail sites in this area.

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In July 2011, Sunoco completed the sale of its phenol and acetone chemical manufacturing facility in Philadelphia, PA (Frankford Facility) and related inventory to an affiliate of Honeywell International Inc. Sunoco received total cash proceeds of \$87 million which is subject to an inventory adjustment subsequent to closing. In connection with this agreement, Sunoco recorded a \$118 million provision (\$70 million after tax) to write down Frankford Facility assets to their estimated fair values during the second quarter of 2011. At June 30, 2011, the carrying amounts were \$73 million for the Frankford Facility and \$45 million for related inventory and other assets. Such amounts have been classified as assets held for sale in the condensed consolidated balance sheet. The results of operations for the Frankford Facility have not been classified as discontinued

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operations due to Sunoco's continuing involvement with the Frankford Facility through a cumene supply agreement which expires December 31, 2016. Upon six months prior notice, Sunoco may terminate this supply agreement on or after July 1, 2012 if a reconfiguration of its Philadelphia refinery results in a reduction in the production of cumene or raw materials necessary to make cumene. The charge is included in the provision for asset write-downs and other matters in the condensed consolidated statements of operations.

Asset Write-Downs and Other Matters

The following table summarizes information regarding the provision for asset write-downs and other matters recognized during the six months ended June 30, 2011 and 2010 (in millions of dollars):

	Pretax	After-tax
2011		
Frankford chemical facility	\$ 118	\$ 70
Haverhill chemical facility	169	101
Eagle Point refinery	5	3
Business improvement initiatives	8	5
	\$ 300	\$ 179
2010		
Eagle Point refinery	\$ 33	\$ 20
Business improvement initiatives	34	20
	\$ 67	\$ 40

In connection with the sale of the Frankford Facility, the Company is evaluating its strategic options with regard to its Haverhill phenol chemical operations (Haverhill Facility) including a potential sale. As a result, the Company evaluated the Haverhill Facility for potential impairment as of June 30, 2011. Sunoco analyzed the expected cash flows of the Haverhill Facility using a probability-weighted analysis which considered the alternatives of continuing to operate and selling the facility. Expected future cash flows associated with the continued operations of the Haverhill Facility were developed using management's estimates about the future operations, including expected production and sales volumes and prices for key raw materials and phenol and related products. Based upon this analysis, Sunoco determined that the long-lived assets at the Haverhill Facility were impaired. The fair value of the Haverhill Facility was then determined based upon an evaluation of discounted expected future operating cash flows of the Haverhill Facility and offers by potential purchasers. In connection therewith, Sunoco recorded a \$169 million provision (\$101 million after tax) to write down Haverhill Facility assets to their estimated fair values during the second quarter of 2011. Since the fair value was estimated primarily based on unobservable inputs, it was determined to be a level 3 fair value measurement within the fair value hierarchy under current accounting guidance.

In connection with ongoing business improvement initiatives to reduce costs and improve business processes, the Company recorded provisions of \$8 and \$34 million (\$5 and \$20 million after tax) during the first half of 2011 and 2010, respectively, primarily for pension settlement losses and employee terminations and related costs.

As a result of the permanent shutdown of the Eagle Point refinery in December 2009, Sunoco established a \$33 million accrual (\$20 million after tax) primarily for contract losses in connection with excess barge capacity during the first half of 2010. Sunoco also recorded a \$5 million provision (\$3 million after tax) to write down certain Eagle Point storage assets which were taken out of service in the second quarter of 2011.

The following table summarizes the changes in the liability for employee terminations and other exit costs (in millions of dollars):

	Six Months Ended June 30,	
	2011	2010
Balance at beginning of period	\$ 79	\$ 68

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Additional accruals		44
Payments charged against the accruals	(17)	(35)
Balance at end of period	\$ 62	\$ 77

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The following tables summarize the components of pretax income (loss) and income tax expense (benefit) from continuing operations (in millions of dollars):

	Six Months Ended June 30, 2011			Six Months Ended June 30, 2010		
	Pretax Income (Loss)	Tax Expense (Benefit)	After-Tax Income (Loss)	Pretax Income (Loss)	Tax Expense (Benefit)	After-Tax Income (Loss)
Income (loss) attributable to Sunoco, Inc. shareholders before discrete items	\$ (70)	\$ (4)	\$ (66)	\$ 242	\$ 84	\$ 158
Discrete items:						
Sale of Toledo refinery	6	7	(1)			
LIFO inventory gains	42	16	26			
Provision for asset write-downs and other matters	(300)	(121)	(179)	(67)	(27)	(40)
Gain on consolidation of pipeline equity interests	9	3	6			
State deferred income tax adjustment		5	(5)		9	(9)
Other		7	(7)	1	5	(4)
Income attributable to noncontrolling interests	80	5	75	56		56
	\$ (233)	\$ (82)	\$ (151)	\$ 232	\$ 71	\$ 161

	Three Months Ended June 30, 2011			Three Months Ended June 30, 2010		
	Pretax Income (Loss)	Tax Expense (Benefit)	After-Tax Income (Loss)	Pretax Income (Loss)	Tax Expense (Benefit)	After-Tax Income (Loss)
Income attributable to Sunoco, Inc. shareholders before discrete items	\$ 71	\$ 20	\$ 51	\$ 245	\$ 85	\$ 160
Discrete items:						
Sale of Toledo refinery	(9)	(4)	(5)			
LIFO inventory gains						
Provision for asset write-downs and other matters	(294)	(119)	(175)			