Cheniere Energy Partners, L.P.
Form 10-Q
May 09, 2007
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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 March 31, 2007

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 No. 001-33366

Cheniere Energy Partners, L.P.

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of incorporation or organization)

20-5913059

(I.R.S. Employer Identification No.)

700 Milam Street, Suite 800

Houston, Texas

(Address of principal executive offices)

77002

(Zip Code)

(713) 375-5000

(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 ¨ No x

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 ¨ Non-accelerated filer x

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

The issuer had 26,416,357 common units and 135,383,831 subordinated units outstanding as of May 1, 2007.

CHENIERE ENERGY PARTNERS, L.P.

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PART I. FINANCIAL INFORMATION

Item 1. Consolidated Financial Statements

CHENIERE ENERGY PARTNERS, L.P.

A DEVELOPMENT STAGE ENTERPRISE

CONSOLIDATED BALANCE SHEETS

(in thousands, except unit data)

	Cheniere Energy Partners, L.P. March 31, 2007 (unaudited)	Combined Predecessor Entities December 31, 2006
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	$ 12	$ 7
Restricted cash and cash equivalents	209,645	176,324
Interest receivable	4,979	5,226
Advances to affiliate	1,327	379
Prepaid expenses	380	385
TOTAL CURRENT ASSETS	216,343	182,321
NON-CURRENT RESTRICTED CASH AND CASH EQUIVALENTS	895,058	982,613
NON-CURRENT RESTRICTED TREASURY SECURITIES	86,304	
PROPERTY, PLANT AND EQUIPMENT, NET	769,436	651,676
DEBT ISSUANCE COSTS, NET	32,646	33,970
ADVANCES UNDER LONG-TERM CONTRACTS	14,022	7,250
OTHER	211	284
TOTAL ASSETS	$ 2,014,020	$ 1,858,114
LIABILITIES AND PARTNERS CAPITAL (DEFICIT)		
CURRENT LIABILITIES		
Accounts payable	$ 8,546	$ 758
Accounts payable affiliate	70	223
Accrued liabilities	99,554	36,670
Accrued liabilities affiliate	435	652
TOTAL CURRENT LIABILITIES	108,605	38,303
LONG-TERM DEBT	2,032,000	2,032,000
DEFERRED REVENUE	40,000	40,000
PAYABLE TO AFFILIATE	15	
OTHER NON-CURRENT LIABILITIES	1,154	1,149
COMMITMENTS AND CONTINGENCIES		

PARTNERS CAPITAL (DEFICIT) OR OWNERS DEFICIT		
Owners deficit, including deficit accumulated during development stage of $72,452 at December 31, 2006		(253,338)
Common unitholders (26,416,357 units issued and outstanding at March 31, 2007)	62,891	
Subordinated unitholders (135,383,831 units issued and outstanding at March 31, 2007)	(225,154)	
General partner interest (2% interest with 3,302,045 units issued and outstanding at March 31, 2007)	(5,491)	
TOTAL PARTNERS DEFICIT OR OWNERS DEFICIT	(167,754)	(253,338)
TOTAL LIABILITIES AND PARTNERS DEFICIT OR OWNERS DEFICIT	$ 2,014,020	$ 1,858,114

See accompanying notes to consolidated combined financial statements.

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CHENIERE ENERGY PARTNERS, L.P.

A DEVELOPMENT STAGE ENTERPRISE

CONSOLIDATED COMBINED STATEMENTS OF OPERATIONS

(in thousands, except per unit data)

(unaudited)

	For the Three Months Ended March 31, 2007	For the Three Months Ended March 31, 2006	Period from October 20, 2003 (Date of Inception) to March 31, 2007
REVENUES	$	$	$
EXPENSES			
Legal			2,227
Professional	131	126	1,702
Technical consulting			4,577
Land site rental	401	382	1,916
Depreciation expense	20	10	83
Labor and overhead charge from affiliate	1,324	1,025	8,868
Phase 2 Stage 1 development reimbursement to affiliate			4,527
Other	10	50	427
TOTAL EXPENSES	1,886	1,593	24,327
LOSS FROM OPERATIONS	(1,886)	(1,593)	(24,327)
OTHER INCOME (EXPENSE)			
Interest income	14,845	49	24,293
Interest expense	(25,817)		(41,280)
Loss on early extinguishment of debt			(23,761)
Derivative gain (loss), net		761	(20,234)
TOTAL OTHER INCOME (EXPENSE)	(10,972)	810	(60,982)
NET LOSS	$ (12,858)	$ (783)	$ (85,309)
Less:			
Net loss through March 25, 2007	(12,128)		
Net loss for partners from March 26, 2007 through March 31, 2007	$ (730)		
Allocation of net loss:			
Limited partners interest	(715)		
General partner s interest	(15)		
Net loss for partners	$ (730)		
Basic and diluted net loss per limited partner unit	$		

Weighted average number of limited partner units outstanding from March 26, 2007 through March 31, 2007 used for basic and diluted net loss per unit calculation:	
Common units	26,416
Subordinated units	135,384
	161,800

See accompanying notes to consolidated combined financial statements.

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CHENIERE ENERGY PARTNERS, L.P.

A DEVELOPMENT STAGE ENTERPRISE

CONSOLIDATED COMBINED STATEMENTS OF PARTNERS CAPITAL (DEFICIT)

(in thousands)

(unaudited)

	Owners Equity	Common Units	Subordinated Units	General Partner Units	Total
Balance at October 20, 2003	$	$	$	$	$
Net loss	(2,763)				(2,763)
Balance at December 31, 2003	(2,763)				(2,763)
Distributions	(10,000)				(10,000)
Net loss	(4,654)				(4,654)
Balance at December 31, 2004	(17,417)				(17,417)
Capital contributions	161,562				161,562
Rescinded distribution	10,000				10,000
Change in fair value of derivative instrument	1,814				1,814
Net loss	(4,263)				(4,263)
Balance at December 31, 2005	151,696				151,696
Capital contributions	35,900				35,900
Distributions	(378,348)				(378,348)
Change in fair value of derivative instrument	(1,814)				(1,814)
Net loss	(60,772)				(60,772)
Balance at December 31, 2006	(253,338)				(253,338)
Net loss through March 25, 2007	(12,128)				(12,128)
Balance at March 25, 2007	(265,466)				(265,466)
Contribution of net deficit investment to unit holders	265,466	(35,434)	(224,556)	(5,476)	
Proceeds from initial public offering, net of issuance costs		98,442			98,442
Net loss from March 26, 2007 through March 31, 2007		(117)	(598)	(15)	(730)
Balance at March 31, 2007	$	$ 62,891	$ (225,154)	$ (5,491)	$ (167,754)

See accompanying notes to consolidated combined financial statements.

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CHENIERE ENERGY PARTNERS, L.P.

A DEVELOPMENT STAGE ENTERPRISE

CONSOLIDATED COMBINED STATEMENTS OF CASH FLOWS

(in thousands)

(unaudited)

	Three Months Ended March 31,		Period from October 20, 2003 (Date of Inception) to March 31,
	2007	2006	2007
CASH FLOWS FROM OPERATING ACTIVITIES			
Net loss	$ (12,858)	$ (783)	$ (85,309)
Adjustments to reconcile net loss to net cash used in operating activities:			
Depreciation	20	10	83
Non-cash derivative gain		(676)	
Non-cash restricted interest income	(14,845)		(23,910)
Amortization of debt issuance costs	950		1,645
Loss on early extinguishment of debt			23,750
Changes in operating assets and liabilities:			
Interest receivable		(1)	
Accounts payable and accrued liabilities	26,551	(877)	40,540
Accounts payable and accrued liabilities affiliate	(217)		435
Deferred revenue			40,000
Payable to affiliate	70		70
Other	10	(895)	231
NET CASH USED IN OPERATING ACTIVITIES	(319)	(3,222)	(2,465)
CASH FLOWS FROM INVESTING ACTIVITIES			
Use of (investment in) restricted cash and cash equivalents	81,465	8,500	(1,073,634)
Investment in restricted treasury securities	(98,442)		(98,442)
LNG terminal construction-in-progress	(73,015)	(78,499)	(697,899)
Advances to EPC contractor, net of transfers to construction-in-progress		8,087	
Advances under long-term contracts	(6,555)		(13,317)
Other	(948)	(107)	(1,327)
NET CASH USED IN INVESTING ACTIVITIES	(97,495)	(62,019)	(1,884,619)
CASH FLOWS FROM FINANCING ACTIVITIES			
Proceeds from issuance of senior notes			2,032,000
Net proceeds from issuance of common units	98,442		98,442
Debt issuance costs	(634)	(4,762)	(61,694)
Proceeds from subordinated note affiliate			37,377
Repayment of subordinated note affiliate			(37,377)
Borrowings from Sabine Pass credit facility		70,000	383,400
Repayment of Sabine Pass credit facility			(383,400)
Distribution to owners			(378,348)
Affiliate payable	11	5	15
Capital contributions by owners			196,681

NET CASH PROVIDED BY FINANCING ACTIVITIES		97,819		65,243		1,887,096
NET INCREASE IN CASH AND CASH EQUIVALENTS		5		2		12
CASH AND CASH EQUIVALENTS beginning of period		7		5		
CASH AND CASH EQUIVALENTS end of period	$	12	$	7	$	12

See accompanying notes to consolidated combined financial statements.

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CHENIERE ENERGY PARTNERS, L.P.

A DEVELOPMENT STAGE ENTERPRISE

NOTES TO CONSOLIDATED COMBINED FINANCIAL STATEMENTS

(unaudited)

NOTE 1 Nature of Operations and Basis of Presentation

Cheniere Energy Partners, L.P. (Cheniere Partners) is a publicly-held limited partnership. As of March 31, 2007, Cheniere Energy, Inc. (Cheniere Energy) owned 91.8% of the partnership through its wholly-owned subsidiaries, Cheniere LNG Holdings, LLC (Holdings) and Cheniere Energy Partners GP, LLC (the General Partner). Cheniere Partners is a Delaware limited partnership formed on November 21, 2006 to develop, own and operate the Sabine Pass liquefied natural gas (LNG) receiving and regasification facility in western Cameron Parish, Louisiana on the Sabine Pass Channel (the Sabine Pass LNG receiving terminal). Cheniere Partners and Holdings, as a selling unitholder, completed an initial public offering (the Offering) of Cheniere Partners common units on March 26, 2007.

The following entities were included on a combined basis in the accompanying Consolidated Combined Financial Statements for periods prior to the Offering because they were entities under common control:

Cheniere Partners;

Cheniere Energy Investments, LLC (Cheniere Investments) is a Delaware limited liability company owned by Cheniere Partners and was formed on November 21, 2006 to hold 100% of the ownership interests in Sabine Pass GP and Sabine Pass LP;

Sabine Pass LNG-GP, Inc. (Sabine Pass GP) is a Delaware corporation that was owned by Holdings and was formed in 2004 to be the general partner of Sabine Pass LNG, L.P. (Sabine Pass LNG);

Sabine Pass LNG-LP, LLC (Sabine Pass LP) is a Delaware limited liability company that was owned by Holdings and was formed in 2004 to be the limited partner of Sabine Pass LNG; and

Sabine Pass LNG is a Delaware limited partnership, formed with one general partner, Sabine Pass GP, and one limited partner, Sabine Pass LP, which owns the entire interest in the Sabine Pass LNG receiving terminal. Sabine Pass LNG is in the development stage, and the purpose of this limited partnership is to own and operate the Sabine Pass LNG receiving terminal.

At the closing of the Offering on March 26, 2007, the equity interests in Sabine Pass GP and Sabine Pass LP were contributed to Cheniere Investments, thereby resulting in Sabine Pass GP, Sabine Pass LP and Sabine Pass LNG becoming indirect, wholly-owned subsidiaries of Cheniere Partners. From and after the closing of the Offering, Cheniere Investments and these subsidiaries are consolidated with Cheniere Partners in the accompanying financial statements. As used in these Notes to Consolidated Combined Financial Statements, the terms Cheniere Partners , we , us and our refer to Cheniere Partners and its consolidated subsidiaries effective with the closing of the Offering and the foregoing entities on a combined basis (the Combined Predecessor Entities) prior to the closing of the Offering.

With the exception of Sabine Pass GP, we are not subject to either federal or state income tax, as the partners are taxed individually on their proportionate share of our earnings. Sabine Pass GP is a corporation and is subject to both federal and state income tax. However, since Sabine Pass GP s inception, its activities have been strictly limited to holding a non-income or loss bearing general partner interest in Sabine Pass LNG and thus, this entity has not realized any taxable net income to date and is not expected to realize any taxable net income in the future.

The accompanying unaudited Consolidated Combined Financial Statements of Cheniere Partners have been prepared in accordance with generally accepted accounting principles in the United States (GAAP) for interim

financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In our opinion, all adjustments, consisting only of normal recurring adjustments necessary for a fair presentation, have been included. The Consolidated Combined Financial Statements include our accounts and those of our subsidiaries. All significant intercompany transactions and balances have been eliminated.

Certain reclassifications have been made to conform prior period information to the current presentation, including a $179.0 million reclassification between current Restricted Cash and Cash Equivalents and Non-Current Restricted Cash and Cash Equivalents on our December 31, 2006 Consolidated Balance Sheet. The reclassification had no effect on our overall consolidated financial position, results of operations or cash flows.

The interim financial statements reflect all adjustments which are, in the opinion of management, necessary for a fair presentation of our results for the interim periods. Such adjustments are considered to be of a normal recurring nature. Results of operations for the three months ended March 31, 2007 are not necessarily indicative of the results of operations that will be realized for the year ended December 31, 2007.

For further information, refer to our combined financial statements and footnotes for the year ended December 31, 2006 included in our Registration Statement on Form S-1, as amended, filed with the Securities and Exchange Commission (SEC) and declared effective on March 20, 2007.

New Accounting Pronouncements

In February 2007, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115*. This statement permits entities to choose to measure many financial instruments and certain other items at fair value. The objective is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. This statement is expected to expand the use of fair value measurement, which is consistent with the FASB s long-term measurement objectives for accounting for financial instruments. This statement is effective as of the beginning of an entity s first fiscal year that begins after November 15, 2007, although earlier adoption is permitted. Management has not determined the effect that adopting this statement would have on our financial condition or results of operations.

NOTE 2 Development Stage Operations

We were formed on October 20, 2003 (the earliest formation date of the Combined Predecessor Entities). Operations to date have been devoted to pre-construction and construction activities. Our ultimate profitability will depend on, among other factors, the successful completion of construction of the Sabine Pass LNG receiving terminal and commencement of commercial operation, which is not expected until the second quarter of 2008 at the earliest. As of March 31, 2007, we had a cumulative deficit of $85.3 million.

NOTE 3 Initial Public Offering

Cheniere Partners and Holdings, as a selling unitholder, completed the Offering of 13,500,000 Cheniere Partners common units for $21.00 per common unit on March 26, 2007. Cheniere Partners received $98.4 million of net proceeds, after deducting the underwriting discount and structuring fee, upon its issuance of 5,054,164 common units to the public in the Offering. Holdings received $164.5 million of net proceeds, after deducting the underwriting discount and structuring fee, upon its sale of 8,445,836 common units. We did not receive any proceeds from this sale of common units by Holdings. Our common units are traded on the American Stock Exchange under the symbol CQP .

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Upon the closing of the Offering on March 26, 2007, the following transactions occurred:

- Holdings contributed through us to our wholly-owned subsidiary, Cheniere Investments, all of its equity interests in Sabine Pass GP and Sabine Pass LP, which own all of the equity interests in Sabine Pass LNG;

- Cheniere Partners issued to Holdings 21,362,193 common units and 135,383,831 subordinated units;

- Cheniere Partners issued to our general partner, a direct wholly-owned subsidiary of Holdings, 3,302,045 general partner units representing a 2% general partner interest in us and all of our incentive distribution rights, which will entitle our general partner to increasing percentages of the cash that we distribute in excess of $0.489 per unit per quarter;

- we issued 5,054,164 common units to the public in the Offering;

- Holdings sold 8,445,836 common units to the public in the Offering, after which Holdings and the public held an aggregate 89.8% and 8.2% limited partner interest in us, respectively;

- our general partner entered into a services agreement with an affiliate of Cheniere Energy under which the affiliate will provide various general and administrative services for an annual administrative fee of $10.0 million (adjusted for inflation after January 1, 2007), with payment commencing January 1, 2009; and

- our general partner entered into a services and secondment agreement with an affiliate of Cheniere pursuant to which we anticipate that certain employees of the Cheniere Energy affiliate will be seconded to our general partner to provide operating and routine maintenance services with respect to the Sabine Pass LNG receiving terminal.

We used all of our net proceeds of $98.4 million from the sale of our common units in the Offering to purchase U.S. treasury securities to fund a distribution reserve to pay quarterly distributions of $0.425 per common unit, as well as related distributions to our general partner, through June 30, 2009.

NOTE 4 Restricted Cash, Cash Equivalents and Treasury Securities

In November 2006, we consummated a private offering of an aggregate principle amount of $2.0 billion of senior secured notes consisting of $550 million of 7 1/4% Senior Secured Notes due 2013 (the 2013 Notes) and $1.5 billion of 7 1/2% Senior Secured Notes due 2016 (the 2016 Notes and, collectively with the 2013 Notes, the Sabine Pass LNG notes) (see Note 7 Long-Term Debt). Under the terms and conditions of the Sabine Pass LNG notes, we were required to fund cash reserve accounts for approximately $335 million related to future interest payments through May 2009 and approximately $887 million to pay the remaining costs to complete the initial phase (Phase 1) and the first stage of the second phase (Phase 2 Stage 1) of the Sabine Pass LNG receiving terminal. These cash accounts are controlled by a collateral trustee, and therefore, are shown as Restricted Cash and Cash Equivalents on the accompanying Consolidated Balance Sheet. As of March 31, 2007 and December 31, 2006, $209.6 million and $176.3 million, respectively, related to future interest payments due within one year and accrued construction costs have been classified as a current asset, and $895.1 million and $982.6 million, respectively, related to remaining construction costs and future interest payments due beyond one year have been classified as a non-current asset on the accompanying Consolidated Balance Sheets.

As discussed above in Note 3, at the closing of the Offering, we funded a distribution reserve for $98.4 million, which was invested in U.S. treasury securities. The distribution reserve, including interest earned, will be used to pay quarterly distributions of $0.425 per common unit for all common units, as well as related distributions to our general partner, through June 30, 2009. The U.S. treasury securities were acquired at a discount from their maturity values equal to an average of approximately 4.87% per year. As of March 31, 2007, we have classified $86.3 million of the U.S. treasury securities as Non-Current Restricted Treasury Securities on our Consolidated Balance Sheet, as these securities have maturities greater than three months. The remaining $12.1 million invested in U.S. treasury securities are classified as Non-Current Restricted Cash and Cash Equivalents on our Consolidated Balance Sheet as of March 31, 2007, as these securities have maturities less than or equal to three months.

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NOTE 5 Property, Plant and Equipment

Property, plant and equipment is comprised of LNG terminal construction-in-progress expenditures, LNG site and related costs and fixed assets, as follows (in thousands):

	March 31, 2007	December 31, 2006
LNG TERMINAL COSTS		
LNG terminal construction-in-progress	$ 769,028	$ 651,369
LNG site and related costs, net	196	197
Total LNG terminal costs	769,224	651,566
FIXED ASSETS		
Computer and office equipment	85	31
Computer software	36	33
Leasehold improvements	10	10
Vehicles	164	99
Accumulated depreciation	(83)	(63)
Total fixed assets, net	212	110
PROPERTY, PLANT AND EQUIPMENT, NET	$ 769,436	$ 651,676

Once the Sabine Pass LNG receiving terminal is placed into service, the LNG terminal construction-in-progress costs will be depreciated using the straight-line depreciation method. We are in the process of determining the most appropriate approach in grouping identifiable components with similar estimated useful lives. Estimated useful lives for components, once construction is completed, are currently estimated to range between 10 and 50 years.

In February 2005 and July 2006, Phase 1 and Phase 2 Stage 1, respectively, of the Sabine Pass LNG receiving terminal satisfied the criteria for capitalization. Accordingly, costs associated with the construction of Phase 1 and Phase 2 Stage 1 of the Sabine Pass LNG receiving terminal have been capitalized as construction-in-progress since those dates. During the three months ended March 31, 2007 and 2006, we capitalized $12.9 million and $2.8 million, respectively, of interest expense, which consisted primarily of interest expense qualifying to be capitalized, amortization of debt issuance costs and commitment fees under the Sabine Pass LNG notes during the three months ended March 31, 2007 and a Sabine Pass LNG credit facility during the three months ended March 31, 2006.

NOTE 6 Accrued Liabilities

Accrued liabilities consisted of the following (in thousands):

	March 31, 2007	December 31, 2006
Interest and related debt fees	$ 59,571	$ 21,815
LNG terminal construction costs	39,873	13,899
Affiliate	435	652
Other	110	956
	$ 99,989	$ 37,322

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NOTE 7 Long-Term Debt

As of March 31, 2007 and December 31, 2006, our long-term debt consisted of the following (in thousands):

	March 31, 2007	December 31, 2006
Sabine Pass LNG notes	$ 2,032,000	$ 2,032,000

Sabine Pass LNG Notes

In November 2006, Sabine Pass LNG consummated a private offering of an aggregate principal amount of $2,032 million of Sabine Pass LNG notes, consisting of $550 million of the 2013 notes and $1,482 million of the 2016 notes. We placed $335 million of the net proceeds in a reserve account to fund scheduled interest payments on the Sabine Pass LNG notes through May 2009. We also placed approximately $887 million in a construction account, which, until satisfaction of construction completion milestones, will only be applied to pay construction and startup costs of the Sabine Pass LNG receiving terminal and to pay other expenses incidental for us to complete construction of the project. We used the remaining net proceeds received from the issuance of the Sabine Pass LNG notes to repay indebtedness, to make a distribution to Holdings for the repayment of its outstanding term loan and to pay fees and expenses related to the issuance of the Sabine Pass LNG notes. Our subsidiary, Sabine Pass LNG, has filed a registration statement with the SEC offering to exchange the Sabine Pass LNG notes for a like amount of senior secured notes of Sabine Pass LNG which are registered under the Securities Act of 1933, as amended.

Interest on the Sabine Pass LNG notes is payable semi-annually in arrears on May 30 and November 30 of each year, beginning May 30, 2007. The Sabine Pass LNG notes are secured on a first-priority basis by a security interest in all of Sabine Pass LNG s equity interests and substantially all of its operating assets.

Under the indenture governing the Sabine Pass LNG notes, except for permitted tax distributions, Sabine Pass LNG may not make distributions until certain conditions are satisfied. The indenture requires that Sabine Pass LNG apply its net operating cash flow (i) first, to fund with monthly deposits its next semiannual payment of approximately $75.5 million of interest on the Sabine Pass LNG notes, and (ii) second, to fund a one-time, permanent debt service reserve fund equal to one semiannual interest payment of approximately $75.5 million on the Sabine Pass LNG notes. Distributions from Sabine Pass LNG will be permitted only after Phase 1 target completion, as defined in the indenture governing the Sabine Pass LNG notes, or such earlier date as project revenues are received, upon satisfaction of the foregoing funding requirements, after satisfying a fixed charge coverage ratio test of 2:1 and after satisfying other conditions specified in the indenture.

NOTE 8 Description of Equity Interests

The common units and subordinated units represent limited partner interests in us. The holders of the units are entitled to participate in partnership distributions and exercise the rights and privileges available to limited partners under our partnership agreement.

The common units and general partner units have the right to receive minimum quarterly distributions of $0.425 per unit, plus any arrearages thereon, before any distribution is made to the holders of the subordinated units.

During the subordination period, the subordinated units will not be entitled to receive any distributions until the common units have received $0.425 per unit plus any arrearages from prior quarters. Subordinated units will convert into common units on a one-for-one basis when the subordination period ends. The subordination period will end when we meet financial tests specified in the partnership agreement, but it generally cannot end before June 30, 2008.

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The general partner interest is entitled to at least 2% of all distributions made by us. In addition, the general partner holds incentive distribution rights, which allow the general partner to receive a higher percentage of quarterly distributions of available cash from operating surplus after the minimum distributions have been achieved and as additional target levels are met. The higher percentages range from 15% up to 50%.

NOTE 9 Financial Instruments

The estimated fair value of financial instruments is the amount at which the instrument could be exchanged currently between willing parties. The carrying amounts reported on the Consolidated Balance Sheets for Cash and Cash Equivalents, Restricted Cash and Cash Equivalents, Accounts Receivable and Accounts Payable approximate fair value due to their short-term nature. We use available market data and valuation methodologies to estimate the fair value of debt. This disclosure is presented in accordance with SFAS No. 107, *Disclosures about Fair Value of Financial Instruments*, and does not impact our financial position, results of operations or cash flows.

Financial Instruments (in thousands):

	March 31, 2007		December 31, 2006	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
2013 Notes (1)	$ 550,000	$ 554,125	$ 550,000	$ 547,250
2016 Notes (1)	1,482,000	1,489,410	1,482,000	1,478,295
Restricted Treasury Securities (2)	98,442	98,442		

(1) The fair value of the Sabine Pass LNG notes was based on quotations obtained from broker-dealers who made markets in these and similar instruments as of March 30, 2007 and December 31, 2006.

(2) The fair value of our Restricted Treasury Securities was based on quotations obtained from broker-dealers who made markets in these and similar instruments as of March 30, 2007. This amount includes $12.1 million classified as Non-Current Restricted Cash and Cash Equivalents on our Consolidated Balance Sheet as of March 31, 2007, as these securities have maturities less than or equal to three months.

NOTE 10 Related Party Transactions

As of March 31, 2007 and December 31, 2006, we had $1.3 million and $0.4 million, respectively, of advances to affiliates.

Service Agreements

Operation and Maintenance Agreement

In February 2005, Sabine Pass LNG entered into an Operation and Maintenance Agreement (O&M Agreement) with Cheniere LNG O&M Services, L.P. (O&M Services), an indirect wholly-owned subsidiary of Cheniere Energy. Pursuant to the O&M Agreement, O&M Services has agreed to provide all necessary services required to construct, operate and maintain the Sabine Pass LNG receiving terminal. The O&M Agreement will remain in effect until 20 years after substantial completion of the facility. Prior to substantial completion of the facility, Sabine Pass LNG is required to pay a fixed monthly fee of $95,000 (indexed for inflation). The fixed monthly fee will increase to $130,000 (indexed for inflation) upon substantial completion of the facility, and O&M Services will thereafter be entitled to a bonus equal to 50% of the salary component of labor costs in certain circumstances to be agreed upon between Sabine Pass LNG and O&M Services at the beginning of each operating year. In addition, Sabine Pass LNG is required to reimburse O&M Services for expenditures incurred by O&M Services on behalf of Sabine Pass LNG for operating expenses, which are comprised of labor, maintenance, land lease and insurance expenses and for maintenance capital expenditures.

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Upon the closing of the Offering, O&M Services assigned the O&M Agreement to our general partner, and O&M Services and our general partner entered into a services and secondment agreement pursuant to which certain employees of O&M Services have been seconded to our general partner to provide operating and routine maintenance services with respect to the Sabine Pass LNG receiving terminal under the direction, supervision and control of our general partner. Under this agreement, our general partner pays O&M Services amounts that it receives from Sabine Pass LNG under the O&M Agreement.

Management Services Agreements

In February 2005, Sabine Pass LNG entered into a Management Services Agreement (the Sabine Pass LNG MSA) with its general partner, Sabine Pass LNG GP, Inc., which is a wholly-owned subsidiary of us. Pursuant to the Sabine Pass LNG MSA, Sabine Pass LNG appointed its general partner to manage the construction and operation of the Sabine Pass LNG receiving terminal, excluding those matters provided for under the O&M Agreement. The Sabine Pass LNG MSA terminates 20 years after the commercial start date set forth in the Total TUA. Prior to substantial completion of construction of the Sabine Pass LNG receiving terminal, Sabine Pass LNG is required to pay its general partner a monthly fixed fee of $340,000 (indexed for inflation); thereafter, the monthly fixed fee will increase to $520,000 (indexed for inflation).

In September 2006, the general partner of Sabine Pass LNG entered into a Management Services Agreement with Cheniere LNG Terminals, Inc. (Cheniere Terminals), a wholly-owned subsidiary of Cheniere Energy. Pursuant to this agreement, Cheniere Terminals provides the general partner with technical, financial, staffing and related support necessary to allow it to meet its obligations to Sabine Pass LNG under the Sabine Pass LNG MSA. Under this agreement with Cheniere Terminals, the general partner of Sabine Pass LNG pays Cheniere Terminals amounts that it receives from Sabine Pass LNG for management of the Sabine Pass LNG receiving terminal.

Services Agreement

Our general partner entered into a services agreement with Cheniere Terminals upon the closing of the Offering. Under this agreement, we will pay Cheniere Terminals an annual administrative fee of $10 million (adjusted for inflation after January 1, 2007) commencing January 1, 2009 for the provision of various general and administrative services provided for our benefit and will reimburse Cheniere Terminals for its services in an amount equal to the sum of all out-of-pocket costs and expenses incurred by Cheniere Terminals that are directly related to our business or activities, such as salaries of operational personnel performing services on-site at the Sabine Pass LNG receiving terminal and the cost of their employee benefits, including 401(k) plan, pension and health insurance benefits. The annual administrative fee includes expenses incurred by Cheniere Terminals to perform all technical, commercial, regulatory, financial, accounting, treasury, tax and legal staffing and related support and all management and other services necessary or reasonably requested on behalf of our partnership by our general partner in order to conduct our business as contemplated by our partnership agreement.

Our general partner will also be entitled to a special annual bonus, which is payable in the sole discretion of Sabine Pass LNG, which is controlled by our general partner. These fees and bonus payments do not include substantial reimbursements that we will make to our general partner and its affiliates on an annual basis for expenses incurred on our behalf.

During the three months ended March 31, 2007 and 2006, we paid a management fee of $0.4 million per month as required under the O&M Agreement and the general partner MSA totaling $1.3 million. These costs are included as an overhead charge from affiliates, net of capitalized general and administrative costs, within the accompanying Consolidated Combined Statements of Operations. As of March 31, 2007 and December 31, 2006, we had $0.4 million and $0.7 million, respectively, of accrued liabilities payable to our affiliates related to these management fees.

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NOTE 11 Commitments and Contingencies

Legal Proceedings

We may in the future be involved as a party to various legal proceedings, which are incidental to the ordinary course of business. We regularly analyze current information and, as necessary, provide accruals for probable liabilities on the eventual disposition of these matters. In the opinion of management and legal counsel, as of March 31, 2007 and December 31, 2006, there were no threatened or pending legal matters that would have a material impact on our consolidated combined results of operations, financial position or cash flows.

NOTE 12 Supplemental Cash Flow Information and Disclosures of Non-Cash Transactions

The following table provides supplemental disclosure of cash flow information (in thousands):

	Three Months Ended March 31,		Period from October 20, 2003 (Date of Inception) to March 31,
	2007	2006	2007
Cash paid for interest (1)	$	$ 2,260	$ 14,353
Construction-in-progress additions recorded as accrued liabilities	$ 46,760	$ 15,782	$ 46,760

(1) All cash paid for interest was capitalized as construction-in-progress.

NOTE 13 Subsequent Events

On April 16, 2007, the underwriters of the Offering exercised their over-allotment option to purchase 2,025,000 additional common units, which resulted in net proceeds of approximately $39.4 million to Holdings, as the selling unitholder, and reduced Cheniere Energy s overall ownership interest in us to approximately 90.6%. We did not receive any proceeds from this sale of additional common units by Holdings.

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Item 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS
INFORMATION REGARDING FORWARD-LOOKING STATEMENTS

This quarterly report contains certain statements that are, or may be deemed to be, forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the Securities Act), and Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act). All statements, other than statements of historical fact, included herein or incorporated herein by reference are forward-looking statements. Included among forward-looking statements are, among other things:

- statements regarding our ability to pay distributions to our unitholders;
- statements relating to the construction and operation of the Sabine Pass liquefied natural gas (LNG) receiving terminal, including statements concerning the completion or expansion thereof by certain dates or at all, the costs related thereto and certain characteristics, including amounts of regasification and storage capacity, the number of storage tanks and docks, pipeline deliverability and the number of pipeline interconnections, if any;
- statements relating to the construction and operation of facilities related to the Sabine Pass LNG receiving terminal;
- statements regarding future levels of domestic natural gas production, supply or consumption; future levels of LNG imports into North America; sales of natural gas in North America; and the transportation, other infrastructure or prices related to natural gas, LNG or other energy sources or hydrocarbon products;
- our expected receipt of cash distributions from Sabine Pass LNG;
- statements regarding any financing transactions or arrangements, or ability to enter into such transactions or arrangements;
- statements regarding any terminal use agreement (TUA) or other agreement to be entered into or performed substantially in the future, including any cash distributions and revenues anticipated to be received and the anticipated timing thereof, and statements regarding the amounts of total LNG regasification capacity that are, or may become, subject to TUAs or other contracts;
- statements regarding counterparties to our TUAs, construction contracts and other contracts;
- statements regarding any business strategy, any business plans or any other plans, forecasts, projections or objectives, any or all of which are subject to change;