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

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2006

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 1-16417

VALERO L.P.
(Exact name of registrant as specified in its charter)

Delaware	**74-2956831**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

One Valero Way
San Antonio, Texas
(Address of principal executive offices)
78249
(Zip Code)

Telephone number: (210) 345-2000
(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** ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. The definition of "accelerated filer and large accelerated filer" is in Rule 12b-2 of the Securities Exchange Act. (Check one):

Large accelerated filer ☒ Accelerated filer ☐ 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** ☒

The number of common units outstanding as of May 8, 2006 was 46,809,749.

VALERO L.P. AND SUBSIDIARIES
FORM 10-Q

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PART I – FINANCIAL INFORMATION

Item 1. Financial Statements

VALERO L.P. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(Thousands of Dollars, Except Unit Data)

	March 31, 2006 (Unaudited)	December 31, 2005
Assets		
Current assets:		
Cash and cash equivalents	$ 105,433	$ 36,054
Receivable from Valero Energy	19,780	21,873
Accounts receivable, net of allowance for doubtful accounts of $1,809 and $1,976 as of March 31, 2006 and December 31, 2005, respectively	80,771	110,066
Inventories	14,607	17,473
Other current assets	30,638	30,138
Assets of businesses held for sale	—	79,807
Total current assets	251,229	295,411
Property and equipment, at cost	2,436,299	2,417,529
Accumulated depreciation and amortization	(279,747)	(257,316)
Property and equipment, net	2,156,552	2,160,213
Intangible assets, net	58,427	59,159
Goodwill	771,486	767,587
Investment in joint ventures	73,794	73,986
Deferred charges and other assets, net	11,692	10,636
Total assets	$3,323,180	$3,366,992
Liabilities and Partners' Equity		
Current liabilities:		
Current portion of long-term debt	$ 566	$ 1,046
Payable to Valero Energy	9,223	12,800
Accounts payable	73,367	104,320
Accrued interest payable	9,712	16,391
Accrued liabilities	39,567	46,917
Taxes other than income taxes	8,383	9,013
Income taxes payable	3,923	4,001
Liabilities of businesses held for sale	—	11,100
Total current liabilities	144,741	205,588
Long-term debt, less current portion	1,187,662	1,169,659
Long-term payable to Valero Energy	5,851	5,507
Deferred income taxes	9,477	13,576
Other long-term liabilities	76,969	71,883
Commitments and contingencies (Note 5)		
Partners' equity:		
Common units (37,210,427 outstanding as of March 31, 2006 and December 31, 2005)	1,745,214	1,749,007
Subordinated units (9,599,322 outstanding as of March 31, 2006 and December 31, 2005)	113,149	114,127
General partner's equity	39,184	38,913
Accumulated other comprehensive income (loss)	933	(1,268)
Total partners' equity	1,898,480	1,900,779
Total liabilities and partners' equity	$3,323,180	$3,366,992

See Condensed Notes to Consolidated Financial Statements.

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VALERO L.P. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
(Unaudited, Thousands of Dollars, Except Unit and Per Unit Data)

	Three Months Ended March 31,	
	2006	2005
Revenues:		
Services revenues:		
Third parties	$ 87,258	$ 1,294
Valero Energy	60,671	55,341
Total services revenues	147,929	56,635
Product sales	126,075	—
Total revenues	274,004	56,635
Costs and expenses:		
Cost of product sales	114,218	—
Operating expenses:		
Third parties	50,613	11,644
Valero Energy	20,457	8,041
Total operating expenses	71,070	19,685
General and administrative expenses:		
Third parties	2,860	746
Valero Energy	5,700	2,757
Total general and administrative expenses	8,560	3,503
Depreciation and amortization expense	24,189	8,732
Total costs and expenses	218,037	31,920
Operating income	55,967	24,715
Equity earnings in joint ventures Pipeline Company	1,206	378
Interest and other expenses, net	(15,465)	(5,829)
Income from continuing operations before income tax expense	41,708	19,264
Income tax expense	2,119	—
Income from continuing operations	39,589	19,264
Loss from discontinued operations	(138)	—
Net income	39,451	19,264
Less general partner's interest and incentive distributions	(4,199)	(1,476)
Limited partners' interest in net income	$ 35,252	$ 17,788
Weighted-average units outstanding	46,809,749	23,041,394
Net income per unit applicable to limited partners:		
Continuing operations	$ 0.75	$ 0.77
Discontinued operations	—	—
Net income	$ 0.75	$ 0.77
Cash distributions per unit applicable to limited partners	$ 0.885	$ 0.800

See Condensed Notes to Consolidated Financial Statements.

VALERO L.P. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited, Thousands of Dollars)

	Three Months Ended March 31, 2006	Three Months Ended March 31, 2005
Cash Flows from Operating Activities:		
Net income	$ 39,451	$ 19,264
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	24,189	8,732
Equity income from joint ventures	(1,293)	(378)
Distributions from joint ventures	1,278	—
Changes in operating assets and liabilities:		
Decrease in receivable from Valero Energy	2,093	250
Decrease in accounts receivable	31,738	1,280
Decrease in inventories	2,870	—
Increase in other current assets	(3,412)	(872)
Decrease in payable to Valero Energy	(3,577)	(828)
Decrease in accrued interest payable	(6,679)	(5,485)
Decrease in accounts payable and other accrued liabilities	(27,314)	(4,385)
Decrease in taxes other than income taxes	(295)	(2,393)
Other, net	(1,997)	115
Net cash provided by operating activities	57,052	15,300
Cash Flows from Investing Activities:		
Reliability capital expenditures	(6,164)	(1,425)
Expansion capital expenditures	(9,428)	(2,860)
Pre-acquisition costs – Kaneb	—	(1,954)
Other acquisition	(12,827)	—
Investment in other noncurrent assets	(1,512)	—
Proceeds from sale of Australia and New Zealand subsidiaries	68,628	—
Distributions in excess of equity income from joint ventures	246	—
Other	992	—
Net cash provided by (used in) investing activities	39,935	(6,239)
Cash Flows from Financing Activities:		
Long-term borrowings	34,000	4,000
Long-term debt repayments	(11,480)	(466)
Decrease in cash book overdrafts	(4,273)	—
Distributions to unitholders and general partner	(43,950)	(19,944)
Net cash used in financing activities	(25,703)	(16,410)
Effect of foreign exchange rate changes on cash	(1,905)	—
Net increase (decrease) in cash and cash equivalents	69,379	(7,349)
Cash and cash equivalents at the beginning of the period	36,054	16,147
Cash and cash equivalents at the end of the period	$105,433	$ 8,798
Supplemental cash flow information:		
Cash paid during the period for interest	$ 25,179	$ 11,546
Cash paid during the period for income taxes	$ 1,839	$ —

See Condensed Notes to Consolidated Financial Statements.

VALERO L.P. AND SUBSIDIARIES
CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. ORGANIZATION, OPERATIONS AND ACCOUNTING PRONOUNCEMENTS

Organization and Operations

Valero L.P. is a publicly traded Delaware limited partnership formed in 1999 that completed its initial public offering of common units on April 16, 2001.

As used in this report, references to “we,” “us,” “our” or the “Partnership” collectively refer, depending on the context, to Valero L.P. or a wholly owned subsidiary of Valero L.P.

These unaudited consolidated financial statements include the accounts of the Partnership and subsidiaries in which the Partnership has a controlling interest. Intercompany balances and transactions have been eliminated in consolidation. Investments in 50% or less owned entities are accounted for using the equity method of accounting. Certain previously reported amounts in the 2005 consolidated financial statements have been reclassified to conform to the 2006 presentation.

These unaudited consolidated financial statements have been prepared in accordance with United States generally accepted accounting principles (GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X of the Securities Exchange Act of 1934. Accordingly, they do not include all of the information and notes required by GAAP for complete consolidated financial statements. In the opinion of management, all adjustments considered necessary for a fair presentation have been included. All such adjustments are of a normal recurring nature unless disclosed otherwise. Financial information for the three months ended March 31, 2006 and 2005 included in these Condensed Notes to Consolidated Financial Statements is derived from our unaudited consolidated financial statements. Operating results for the three months ended March 31, 2006 are not necessarily indicative of the results that may be expected for the year ending December 31, 2006.

The consolidated balance sheet as of December 31, 2005 has been derived from the audited consolidated financial statements as of that date. You should read these consolidated financial statements in conjunction with the consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2005.

Our operations are managed by Valero GP, LLC. Valero GP, LLC is the general partner of Riverwalk Logistics, L.P., which is the 2% general partner of Valero L.P. Valero GP, LLC and Riverwalk Logistics, L.P. are indirect wholly owned subsidiaries of Valero Energy Corporation (Valero Energy). Valero Energy, through various affiliates, is also a limited partner in us, resulting in a combined partnership ownership of 23.4%. The remaining 76.6% limited partnership interests are held by public unitholders.

On January 15, 2006, UDS Logistics, LLC, an indirect, wholly owned subsidiary of Valero Energy, changed its name to Valero GP Holdings, LLC (Holdings). On January 25, 2006, Holdings formed Riverwalk Holdings, LLC, a Delaware limited liability company and a direct, wholly owned subsidiary, and contributed its 21.4% limited partnership interest (both common and subordinated units) in Valero L.P. and its 99.9% limited partnership interest in Riverwalk Logistics, L.P. to the newly formed subsidiary.

On March 31, 2006, Holdings filed a registration statement on Form S-1 with the Securities and Exchange Commission for an initial public offering of approximately 37% of its units representing limited liability company interests. All units will be sold by subsidiaries of Valero Energy, which initially will retain an approximate 63% ownership interest in Holdings, the principal owner of our general partner interest and the general partner incentive distribution rights and the owner of 21.4% limited partner interest in us. In the registration statement, Valero Energy states its intention to further reduce and ultimately sell all of its interest in Holdings pending market conditions.

We conduct our operations through our subsidiaries, primarily Valero Logistics Operations, L.P. (Valero Logistics) and Kaneb Pipe Line Operating Partnership, L.P. (KPOP). We have four business segments: refined product terminals, refined product pipelines, crude oil pipelines and crude oil storage tanks.

VALERO L.P. AND SUBSIDIARIES
CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

New Accounting Pronouncements

FASB Statement No. 156

In March 2006, the FASB issued Statement No. 156, "Accounting for Servicing of Financial Assets," which amends Statement No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities." Statement No. 156 requires the initial recognition at fair value of a servicing asset or servicing liability when an obligation to service a financial asset is undertaken by entering into a servicing contract. Statement No. 156 is effective for fiscal years beginning after September 15, 2006, with early adoption permitted. The adoption of Statement No. 156 is not expected to affect our financial position or results of operations.

FASB Statement No. 155

In February 2006, the FASB issued Statement No. 155, "Accounting for Certain Hybrid Financial Instruments," which amends Statement No. 133, "Accounting for Derivative Instruments and Hedging Activities," and Statement No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities." This statement improves the financial reporting of certain hybrid financial instruments and simplifies the accounting for these instruments. In particular, Statement No. 155:

- permits fair value remeasurement for any hybrid financial instrument that contains an embedded derivative that otherwise would require bifurcation,
- clarifies which interest-only and principal-only strips are not subject to the requirements of Statement No. 133,
- establishes a requirement to evaluate interests in securitized financial assets to identify interests that are freestanding derivatives or that are hybrid financial instruments that contain an embedded derivative requiring bifurcation,
- clarifies that concentrations of credit risk in the form of subordination are not embedded derivatives, and
- amends Statement No. 140 to eliminate the prohibition on a qualifying special-purpose entity from holding a derivative financial instrument that pertains to a beneficial interest other than another derivative financial instrument.

Statement No. 155 is effective for all financial instruments acquired or issued after the beginning of an entity's fiscal year that begins after September 15, 2006, and is not expected to affect our financial position or results of operations.

2. ACQUISITIONS

Capwood Pipeline

We purchased a 23.77% interest in Capwood pipeline from Valero Energy for approximately $13.0 million, which was paid from borrowings under our existing revolving credit agreement. The Capwood pipeline is a 57-mile crude oil pipeline that extends from Patoka, Illinois to Wood River, Illinois. Plains All American Pipeline L.P., the operator of the Capwood pipeline, owns the remaining 76.23% interest. Our financial statements include the results of operations of our interest in the Capwood pipeline in the crude oil pipelines segment for the three months ended March 31, 2006.

The purchase price of the Capwood pipeline was primarily allocated to property and equipment. The pro forma financial information for the three months ended March 31, 2005 that give effect to the acquisition of the Capwood pipeline on January 1, 2005 has not been disclosed as the effect is not significant.

Kaneb Acquisition

On July 1, 2005, we completed our acquisition (the Kaneb Acquisition) of Kaneb Services LLC (KSL) and Kaneb Pipe Line Partners, L.P. (KPP, and, together with KSL, Kaneb).

The Kaneb Acquisition was accounted for using the purchase method. The purchase price has been preliminarily allocated based on the estimated fair values of the individual assets acquired and liabilities assumed at the date of acquisition pending completion of an independent appraisal and other evaluations.

VALERO L.P. AND SUBSIDIARIES
CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The purchase price and the preliminary purchase price allocation as of March 31, 2006 were as follows (in thousands):

Cash paid for the outstanding equity securities of KSL	$ 509,307
Value of Valero L.P.'s common units issued in exchange for KPP common units	1,451,249
Transaction costs	9,403
Fair value of long-term debt assumed	779,707
Fair value of other liabilities assumed	172,687
Total	$2,922,353
Current assets	$ 602,085
Property and equipment	1,428,978
Goodwill	766,771
Intangible assets	58,900
Other noncurrent assets	65,619
Total	$2,922,353

The condensed statements of income include the results of operations of the Kaneb Acquisition commencing on July 1, 2005. As a result, information for the three months ended March 31, 2006 presented below represents actual results of operations. The unaudited pro forma financial information below includes the historical financial information of Kaneb and the Partnership for the period indicated. This financial information assumes the following:

- we completed the Kaneb Acquisition on January 1, 2005;
- we borrowed $525.0 million to purchase all of the outstanding equity securities of KSL,
- we issued approximately 23.8 million common units in exchange for all of the outstanding common units of KPP,
- we received a contribution from our general partner of $29.2 million to maintain its 2% interest;
- and the results of operations of Martin Oil LLC (a marketing subsidiary of KSL), our Australia and New Zealand subsidiaries, and certain assets we divested in conjunction with the Kaneb Acquisition (Held Separate Businesses), are reported as discontinued operations.

The unaudited pro forma information is not necessarily indicative of the results of future operations:

	Three Months Ended March 31, 2006	2005
	(Thousands of Dollars, Except Per Unit Data)	
Revenues	$ 274,004	$ 219,032
Operating income	55,967	45,925
Income from continuing operations	39,589	32,393
Income (loss) from discontinued operations	(138)	3,788
Net income	$ 39,451	$ 36,181
Net income per unit applicable to limited partners:		
Continuing operations	$ 0.75	$ 0.61
Discontinued operations	—	0.08
Net income	$ 0.75	$ 0.69

VALERO L.P. AND SUBSIDIARIES
CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

3. DISPOSITIONS

Sale of Australia and New Zealand subsidiaries

On March 30, 2006, we sold our Australia and New Zealand subsidiaries to ANZ Terminals Pty. Ltd., for total proceeds of $65.0 million, plus working capital. The proceeds will be used for working capital purposes, including paying down outstanding debt. This transaction included the sale of eight terminals with an aggregate storage capacity of 1.1 million barrels. Revenues and pre-tax income related to the Australia and New Zealand subsidiaries, were included in loss from discontinued operations, and totaled $5.0 million and $0.6 million, respectively, for the three months ended March 31, 2006.

4. LONG-TERM DEBT

$400 Million Revolving Credit Agreement

During the three months ended March 31, 2006, we borrowed $34.0 million under our $400 million 2005 revolving credit agreement (the 2005 Revolving Credit Agreement) to fund the purchase of the Capwood pipeline and our capital expenditures. Additionally, we repaid $11.0 million during the three months ended March 31, 2006. The 2005 Revolving Credit Agreement bears interest based on either an alternative base rate or LIBOR, which was 5.5% as of March 31, 2006. As of March 31, 2006, we had $372.1 million available for borrowing under our 2005 Revolving Credit Agreement.

Interest Rate Swaps

As of March 31, 2006, the weighted-average interest rate for our interest rate swaps was 7.1%. As of March 31, 2006 and December 31, 2005, the aggregate estimated fair value of the interest rate swaps included in other long-term liabilities in our consolidated balance sheets was $7.9 million and $4.0 million, respectively.

Other

In Holding's registration statement on Form S-1, Valero Energy stated its intention to ultimately sell of its interest in Holdings pending market conditions. If Valero Energy ultimately sells all of its interests in Holdings, it will no longer own our general partner, which would trigger certain requirements in our debt instruments. As a result, we took the following actions:

- On April 19, 2006, Valero Logistics commenced a consent solicitation from the holders of its $100.0 million 6.875% senior notes due 2012 and its $250.0 million 6.05% senior notes due 2013 in order to amend the change of control covenant requiring that Valero Energy or an investment grade entity own 51% of our general partner interest as set forth in the indenture governing the notes of both such series. Holders of record as of April 18, 2006 who consent to the proposed amendment will receive $5.00 per $1,000 principal amount with respect to 6.05% Senior Notes and $2.50 per $1,000 principal amount with respect to the 6.875% senior notes. The consent solicitation will expire on May 10, 2006, unless further extended.
- In May 2006, we initiated discussions to amend the 2005 Revolving Credit Agreement, the $525 Term Loan Agreement and the UK Term Loan in order to eliminate the change in control provision requiring Valero Energy to own at least a majority of the outstanding equity interests in our general partner.

5. COMMITMENTS AND CONTINGENCIES

Litigation and Environmental Matters

We have contingent liabilities resulting from various litigation, claims and commitments, the most significant of which are discussed below. We record accruals for loss contingencies when losses are considered probable and can be reasonably estimated. Legal fees associated with defending ourselves in legal matters are expensed as incurred. As of March 31, 2006, we have recorded accruals for contingent losses, including settled matters, totaling $51.9 million. The actual payment of any amounts accrued and the timing of any such payments ultimately made is uncertain. We believe that should we be unable to successfully defend ourselves in any of these matters, the ultimate payment of any or all of the amounts reserved would not have a material adverse effect on our financial position or liquidity. However, if any actual losses ultimately exceed the amounts accrued, there could be a material adverse effect on our results of operations.

Grace Energy Corporation Matter. In 1997, Grace Energy Corporation (Grace Energy) sued subsidiaries of Kaneb in Texas state court. The complaint sought recovery of the cost of remediation of fuel leaks in the 1970s from a pipeline that had once connected a former Grace Energy terminal with Otis Air Force Base in Massachusetts (Otis AFB). Grace Energy alleges the Otis AFB pipeline and related environmental liabilities had been transferred in 1978 to an entity that was part of Kaneb's acquisition of Support Terminal Services, Inc. and its subsidiaries from Grace Energy in 1993. Kaneb contends that it did not acquire the Otis AFB pipeline and never assumed any responsibility for any associated environmental damage.

VALERO L.P. AND SUBSIDIARIES
CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

In 2000, the court entered final judgment that: (i) Grace Energy could not recover its own remediation costs of $3.5 million, (ii) Kaneb owned the Otis AFB pipeline and its related environmental liabilities and (iii) Grace Energy was awarded $1.8 million in attorney costs. Both Kaneb and Grace Energy appealed the trial court's final judgment to the Texas Court of Appeals in Dallas. In 2001, Grace Energy filed a petition in bankruptcy, which created an automatic stay of actions against Grace Energy. Once that stay is lifted, we intend to resume vigorous prosecution of the appeal.

The Otis AFB is a part of a Superfund Site pursuant to the Comprehensive Environmental Response Compensation and Liability Act (CERCLA). The site contains a number of groundwater contamination plumes, two of which are allegedly associated with the Otis AFB pipeline. Relying on the Texas state court's final judgment assigning ownership of the Otis AFB pipeline to Kaneb, the U.S. Department of Justice advised Kaneb in 2001 that it intends to seek reimbursement from Kaneb for the remediation costs associated with the two spill areas. In 2002, the Department of Justice asserted that it had incurred over $49.0 million in costs and expected to incur additional costs of approximately $19.0 million for remediation of the two spill areas. The Department of Justice has not filed a lawsuit against us on this matter and we have not made any payments toward costs incurred by the Department of Justice.

Port of Vancouver Matter. We own a chemical and refined products terminal on property owned by the Port of Vancouver, and we lease the land under the terminal from the Port of Vancouver. Under an Agreed Order entered into with the Washington Department of Ecology when Kaneb purchased the terminal in 1998, Kaneb agreed to investigate and remediate groundwater contamination by the terminal's previous owner and operator originating from the terminal. Investigation and remediation at the terminal are ongoing, in compliance with the Agreed Order. In April 2006, the Washington Department of Ecology commented on our site investigation work plan and asserted that the groundwater contamination at the terminal was commingled with a groundwater contamination plume under other property owned by the Port of Vancouver. We dispute this assertion. No lawsuits have been filed against us in this matter, and our liability for any portion of total future remediation costs of the commingled plume is not reasonably estimable at this time. Factors that could affect estimated remediation costs include whether Kaneb will be found to have ultimate responsibility for some portion of the commingled plume, the Port of Vancouver's contribution to the remediation effort and the amount the Port of Vancouver actually receives from other potentially responsible parties.

Xanser Tax Indemnification. In 2001, Xanser, Inc (Xanser) distributed its interest in its pipeline, terminalling and product marketing business to its shareholders, which resulted in the formation of KSL. Pursuant to that distribution, KSL agreed to indemnify Xanser for certain potential tax liabilities, if any, that resulted from the distribution.

St. Eustatius Tax Agreement. On June 1, 1989, the governments of the Netherlands Antilles and St. Eustatius approved a Free Zone and Profit Tax Agreement retroactive to January 1, 1989, which expired on December 31, 2000. This agreement required a subsidiary of Kaneb, which we acquired on July 1, 2005, to pay the greater of 2% of taxable income, as defined therein, or 500,000 Netherlands Antilles guilders (approximately $0.3 million) per year. The agreement further provided that any amounts paid in order to meet the minimum annual payment were available to offset future tax liabilities under the agreement to the extent that the minimum annual payment is greater than 2% of taxable income.

On February 22, 2006, we entered into a revised agreement (the 2005 Tax and Maritime Agreement) with the governments of St. Eustatius and the Netherlands Antilles. The 2005 Tax and Maritime Agreement is effective beginning January 1, 2005 and expires on December 31, 2014. Under the terms of the 2005 Tax and Maritime Agreement, we agreed to make a one-time payment of five million Netherlands Antilles guilders (approximately $2.8 million) in full and final settlement of all of our liabilities, taxes, fees, levies, charges, or otherwise (including settlement of audits) due or potentially due to St. Eustatius. We further agreed to pay an annual minimum profit tax to St. Eustatius of one million Netherlands Antilles guilders (approximately $0.6 million), beginning as of January 1, 2005. We agreed to pay the minimum annual profit tax in twelve equal monthly installments. To the extent the minimum annual profit tax exceeds 2% of taxable profit (as defined in the 2005 Tax and Maritime Agreement), we can carry forward that excess to offset future tax liabilities. If the minimum annual profit tax is less than 2% of taxable profit, we agreed to pay that difference.

We are also a party to additional claims and legal proceedings arising in the ordinary course of business. We believe the possibility is remote that the final outcome of any of these claims or proceedings to which we are a party would

VALERO L.P. AND SUBSIDIARIES
CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

have a material adverse effect on our financial position, results of operations or liquidity; however, due to the inherent uncertainty of litigation, there can be no assurance that the resolution of any particular claim or proceeding would not have a material adverse effect on our results of operations, financial position or liquidity.

Commitment

On April 13, 2006, we entered into an agreement to purchase three 30,000 barrel and two 52,000 barrel tank barges over the next two years. The contract price is $34.1 million, which is subject to adjustment based on the actual cost incurred for the steel.

6. RELATED PARTY TRANSACTIONS

We have related party transactions with Valero Energy for pipeline tariff, terminalling fee and crude oil storage tank fee revenues, which are comparable to the fees charged to third parties for similar services. In addition, we reimburse Valero Energy for the actual costs of Valero Energy employees working solely on our behalf and for charges incurred on our behalf.

Additionally, Valero Energy charges us an administrative service fee for certain administrative functions, primarily information systems support, ad valorem taxes, risk management, and human resources administration. If we cease to obtain such administrative services from Valero Energy our results of operations may be adversely impacted.

The receivable from Valero Energy as of March 31, 2006 and December 31, 2005 represents amounts due for pipeline tariff, terminalling fee and crude oil storage tank fee revenues and the payable to Valero Energy primarily represents amounts due for employee costs and the administrative service fee.

The following table summarizes information pertaining to transactions with Valero Energy:

	Three Months Ended March 31,	
	2006	2005
	(Thousands of Dollars)	
Revenues	$60,671	$55,341
Operating expenses	20,457	8,041
General and administrative expenses	5,700	2,757

Our share of allocated Valero Energy employee benefit plan expenses, excluding compensation expense related to restricted common units and unit options, was $7.8 million and $2.9 million for the three months ended March 31, 2006 and 2005, respectively. These employee benefit plan expenses and the related payroll costs are included in operating expenses and general and administrative expenses.

Services Agreement

For the three months ended March 31, 2005, Valero Energy charged us $0.3 million for administrative services. Effective July 1, 2005, the Services Agreement was amended (the 2005 Services Agreement) to account for our significant growth following the closing of the Kaneb Acquisition resulting in an increase in the administrative fee to $13.8 million for the first year from July 1, 2005 to June 30, 2006.

Effective January 1, 2006, pursuant to a new services agreement (2006 Services Agreement), Valero GP, LLC began directly performing many of the services previously provided by Valero Energy under the 2005 Services Agreement, primarily consisting of information systems, legal, corporate development and health, safety and environmental functions. The employees performing these services became employees of Valero GP, LLC, and their costs are now directly charged to us. Accordingly, the annual fee charged to us by Valero Energy for administrative services was reduced from $13.8 million to approximately $1.9 million per year. This annual fee will increase to approximately $2.9 million and $3.4 million in 2007 and 2008, respectively. The annual fee will remain at approximately $3.4 million through the term of the agreement. In addition, each annual fee will be subject to adjustments to account for Valero Energy’s annual salary increase. Subject to approval by our Conflicts Committee, the amounts may also be adjusted for changed service levels.

The 2006 Services Agreement will expire on December 31, 2010 with automatic two-year renewal options unless terminated by either party at least six months prior to the renewal period. We may cancel or reduce the level of services that Valero Energy provides us on 60 days prior written notice. The 2006 Services Agreement will terminate upon the change of control of either Valero Energy or us.

New Omnibus Agreement

On March 31, 2006, Valero L.P. entered into an amended and restated omnibus agreement (the New Omnibus Agreement) with Valero Energy, Valero GP, LLC, Riverwalk Logistics, L.P., and Valero Logistics. The New Omnibus Agreement amended certain definitions and other provisions in the April 16, 2001 omnibus agreement, which it supersedes, to clarify the parties' intent as to the Valero Energy ownership requirements for the application of the business restrictions described below.

Under the New Omnibus Agreement, Valero Energy has agreed, and will cause its controlled affiliates to agree, for so long as Valero Energy owns 20% or more of us or our general partner, not to engage in the business of transporting crude oil and other feedstocks or refined products, including petrochemicals, or operating crude oil storage facilities or refined product terminalling assets in the United States. This restriction does not apply to:

- any business retained by Ultramar Diamond Shamrock (UDS) as of April 16, 2001, the closing of our initial public offering, or any business owned by Valero Energy at the date of its acquisition of UDS on December 31, 2001;
- any business with a fair market value of less than $10 million;
- any business acquired by Valero Energy in the future that constitutes less than 50% of the fair market value of a larger acquisition, provided we have been offered and declined the opportunity to purchase the business; and
- any newly constructed pipeline, terminalling or storage assets that we have not offered to purchase at fair market value within one year of construction.

Also under the New Omnibus Agreement, Valero Energy has agreed to indemnify us for environmental liabilities related to the assets transferred to us in connection with our initial public offering, provided that such liabilities arose prior to and are discovered within ten years after that date (excluding liabilities resulting from a change in law after April 16, 2001).

7. PARTNERS' EQUITY

Outstanding Equity

We have identified our general partner interest and subordinated units as participating securities and we use the two-class method when calculating "net income per unit applicable to limited partners," which is based on the weighted-average number of common and subordinated units outstanding during the period. Net income per unit applicable to limited partners is computed by dividing net income applicable to limited partners, after deducting the general partner's 2% interest and incentive distributions, by the weighted-average number of limited partnership units outstanding. Basic and diluted net income per unit applicable to limited partners is the same because we have no potentially dilutive securities outstanding.

Cash Distributions

On January 27, 2006, we declared a quarterly cash distribution of $0.855 per unit paid on February 14, 2006 to unitholders of record on February 7, 2006, which totaled $44.0 million. On April 18, 2006, we declared a quarterly cash distribution of $0.885 per unit to be paid on May 12, 2006 to unitholders of record on May 5, 2006, which totaled $45.8 million.

VALERO L.P. AND SUBSIDIARIES
CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The following table reflects the allocation of total cash distributions to the general and limited partners applicable to the period in which the distributions were earned:

	Three Months Ended March 31, 2006	2005
	(Thousands of Dollars, Except Per Unit Data)	
General partner interest	$ 916	$ 399
General partner incentive distribution	3,480	1,112
Total general partner distribution	4,396	1,511
Limited partners' distribution	41,427	18,433
Total cash distributions	$ 45,823	$ 19,944
Cash distributions per unit applicable to limited partners	$ 0.885	$ 0.800

Subordinated Units

We satisfied all the conditions included in our partnership agreement for the subordination period to end. Accordingly, the subordination period ended effective April 1, 2006 and all 9,599,322 subordinated units converted into common units on a one-for-one basis on May 8, 2006, the first business day after the record date for the distribution related to the first quarter earnings of 2006. Riverwalk Holdings, LLC held the 9,599,322 subordinated units at the time of conversion.

Comprehensive Income

For the three months ended March 31, 2006, the difference between our net income and our comprehensive income resulted from foreign currency translation adjustments. Our total comprehensive income was as follows:

	Three Months Ended March 31, 2006	2005
	(Thousands of Dollars)	
Net income	$ 39,451	$ 19,264
Foreign currency translation adjustment	2,201	—
Comprehensive income	$ 41,652	$ 19,264

8. SEGMENT INFORMATION

Our operating segments consist of refined product terminals, refined product pipelines, crude oil pipelines and crude oil storage tanks. The operations related to the Kaneb Acquisition on July 1, 2005 principally involve transporting refined petroleum products and fertilizer as a common carrier, the storage of petroleum products, specialty chemicals, and other liquids. In addition, we also deliver and sell bunker fuel at St. Eustatius, Netherlands Antilles and Point Tupper, Nova Scotia. The results of Kaneb's transportation operations are included in our refined product pipelines segment. The results of Kaneb's storage and bunker fuel operations are included in our refined product terminals segment.

VALERO L.P. AND SUBSIDIARIES
CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Results of operations for the reportable segments were as follows:

	Three Months Ended March 31, 2006	Three Months Ended March 31, 2005
	(Thousands of Dollars)	
Revenues:		
Refined product terminals	$ 196,148	$ 9,937
Refined product pipelines	52,046	22,182
Crude oil pipelines	14,049	13,185
Crude oil storage tanks	11,761	11,331
Total revenues	$ 274,004	$ 56,635
Operating income:		
Refined product terminals	$ 27,045	$ 3,581
Refined product pipelines	22,105	9,022
Crude oil pipelines	9,103	8,216
Crude oil storage tanks	6,274	7,399
Total segment operating income	64,527	28,218
Less general and administrative expenses	8,560	3,503
Total operating income	$ 55,967	$ 24,715

Revenues from Valero Energy by operating segment were as follows:

	Three Months Ended March 31, 2006	Three Months Ended March 31, 2005
	(Thousands of Dollars)	
Revenues:		
Refined product terminals	$ 11,019	$ 9,790
Refined product pipelines	24,356	21,035
Crude oil pipelines	13,535	13,185
Crude oil storage tanks	11,761	11,331
Total revenues	$ 60,671	$ 55,341

Total assets by reportable segment were as follows:

	March 31, 2006	December 31, 2005
	(Thousands of Dollars)	
Refined product terminals	$1,587,257	$1,701,782
Refined product pipelines	1,293,179	1,286,571
Crude oil pipelines	123,320	123,698
Crude oil storage tanks	202,991	204,580
Total segment assets	3,206,747	3,316,631
General partnership assets assets and other noncurrent assets)	116,433	50,361
Total consolidated assets	$3,323,180	$3,366,992

VALERO L.P. AND SUBSIDIARIES
CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

9. CONDENSED CONSOLIDATING FINANCIAL STATEMENTS

Valero L.P. has no operations and its assets consist mainly of its investments in Valero Logistics, KSL and KPP. KPP is the majority owner of KPOP. Valero Logistics and KPOP are 100% indirectly owned by Valero L.P. Valero Logistics and KPOP own and operate pipelines, terminals and storage tanks and are issuers of publicly traded senior notes. The senior notes issued by Valero Logistics were and continue to be fully and unconditionally guaranteed by Valero L.P. In connection with the Kaneb Acquisition, effective July 1, 2005, Valero L.P. fully and unconditionally guaranteed the outstanding senior notes issued by KPOP. Additionally, effective July 1, 2005, both Valero Logistics and KPOP fully and unconditionally guaranteed the outstanding senior notes of the other. All guarantors are jointly and severally liable for performance under the terms of the guarantees.

As a result, the following condensed consolidating financial statements are being presented for the current year as an alternative to providing separate financial statements for Valero Logistics and KPOP. Condensed consolidating statements of income for the comparable periods of 2005 are not presented as we did not own Kaneb.

Condensed Consolidating Balance Sheet
March 31, 2006
(Thousands of Dollars)

	Valero L.P.	Valero Logistics Operations, L.P.	Kaneb Pipe Line Operating Partnership L.P.	Non-Guarantor Subsidiaries (a)	Eliminations	Valero L.P. Consolidated
Assets						
Current assets	$ 43	$ 165,827	$ 629,927	$ 131,330	$ (675,898)	$ 251,229
Property and equipment, net	—	784,678	684,804	687,070	—	2,156,552
Goodwill	—	4,715	194,509	572,262	—	771,486
Investment in wholly owned subsidiaries	2,399,920	31,691	622,813	1,293,346	(4,347,770)	—
Equity investments	—	15,102	—	58,692	—	73,794
Other noncurrent assets, net	228	9,202	722	59,967	—	70,119
Total assets	$2,400,191	$1,011,215	$2,132,775	$2,802,667	$(5,023,668)	$3,323,180
Liabilities and Partners' Equity						
Current liabilities Current liabilities	$ 502,644	$ 36,687	$ 37,634	$ 243,674	$ (675,898)	$ 144,741
Long-term debt, less current portion	—	601,039	550,154	36,469	—	1,187,662
Long-term payable to Valero Energy	—	—	—	5,851	—	5,851
Deferred income taxes	—	—	—	9,477	—	9,477
Other long-term liabilities	—	8,652	4,549	63,768	—	76,969
Total partners' equity	1,897,547	364,837	1,540,438	2,443,428	(4,347,770)	1,898,480
Total liabilities and partners' equity	$2,400,191	$1,011,215	$2,132,775	$2,802,667	$(5,023,668)	$3,323,180

(a) Non-guarantor subsidiaries are wholly owned by Valero L.P., Valero Logistics or KPOP.

VALERO L.P. AND SUBSIDIARIES
CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Condensed Consolidating Balance Sheet
December 31, 2005
(Thousands of Dollars)

	Valero L.P.	Valero Logistics Operations, L.P.	Kaneb Pipe Line Operating Partnership L.P.	Non-Guarantor Subsidiaries (a)	Eliminations	Valero L.P. Consolidated
Assets						
Current assets	$ 44	$ 196,481	$ 622,669	$ 240,741	$ (764,524)	$ 295,411
Property and equipment, net	—	783,945	694,374	681,894	—	2,160,213
Goodwill	—	4,715	193,127	569,745	—	767,587
Investment in wholly owned subsidiaries	2,403,969	16,920	603,474	1,273,313	(4,297,676)	—
Equity investments	—	15,087	—	58,899	—	73,986
Other noncurrent assets, net	228	8,677	771	60,119	—	69,795
Total assets	$2,404,241	$1,025,825	$2,114,415	$ 2,884,711	$(5,062,200)	$3,366,992
Liabilities and Partners' Equity						
Current liabilities Current liabilities	$ 502,194	$ 50,252	$ 40,341	$ 377,325	$ (764,524)	$ 205,588
Long-term debt, less current portion	—	581,921	551,607	36,131	—	1,169,659
Long-term payable to Valero Energy	—	—	—	5,507	—	5,507
Deferred income taxes	—	—	—	13,576	—	13,576
Other long-term liabilities	—	4,821	2,124	64,938	—	71,883
Total partners' equity	1,902,047	388,831	1,520,343	2,387,234	(4,297,676)	1,900,779
Total liabilities and partners' equity	$2,404,241	$1,025,825	$2,114,415	$ 2,884,711	$(5,062,200)	$3,366,992

(a) Non-guarantor subsidiaries are wholly owned by Valero L.P., Valero Logistics or KPOP.

VALERO L.P. AND SUBSIDIARIES
CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Condensed Consolidating Statements of Income
For the Three Months Ended March 31, 2006
(Thousands of Dollars)

	Valero L.P.	Valero Logistics Operations, L.P.	Kaneb Pipe Line Operating Partnership L.P.	Non-Guarantor Subsidiaries (a)	Eliminations	Valero L.P. Consolidated
Revenues	$ —	$ 60,683	$ 27,200	$ 186,371	$ (250)	$ 274,004
Costs and expenses	450	33,398	19,729	164,710	(250)	218,037
Operating income	(450)	27,285	7,471	21,661	—	55,967
Equity earnings	39,901	301	19,339	21,213	(79,548)	1,206
Interest and other expense, net	—	(7,630)	(7,014)	(821)	—	(15,465)
Income from continuing operations before income tax expense	39,451	19,956	19,796	42,053	(79,548)	41,708
Income tax expense	—	—	—	2,119	—	2,119
Income from continuing operations	39,451	19,956	19,796	39,934	(79,548)	39,589
Income from discontinued operations	—	—	298	(436)	—	(138)
Net income	$39,451	$ 19,956	$ 20,094	$ 39,498	$ (79,548)	$ 39,451

(a) Non-guarantor subsidiaries are wholly owned by Valero L.P., Valero Logistics or KPOP.

VALERO L.P. AND SUBSIDIARIES
CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Condensed Consolidating Statement of Cash Flows
For the Three Months Ended March 31, 2006
(Thousands of Dollars)

	Valero L.P.	Valero Logistics Operations, L.P.	Kaneb Pipe Line Operating Partnership L.P.	Non-Guarantor Subsidiaries (a)	Eliminations	Valero L.P. Consolidated
Cash flows from operating activities:						
Net income	$ 39,451	$ 19,956	$ 20,094	$ 39,498	$ (79,548)	$ 39,451
Adjustments to reconcile net income to net cash provided by operating activities:						
Depreciation and amortization	—	8,938	6,045	9,206	—	24,189
Equity income, net of distributions	4,049	(286)	(19,339)	(20,017)	35,593	—
Changes in operating assets and liabilities and other	(2,521)	(10,292)	(7,156)	13,381	—	(6,588)
Net cash provided by (used in) operating activities	40,979	18,316	(356)	42,068	(43,955)	57,052
Cash flows from investing activities:						
Capital expenditures	—	(9,516)	(611)	(5,465)	—	(15,592)
Other acquisition	—	(12,827)	—	—	—	(12,827)
Proceeds from sale of assets	—	—	—	68,628	—	68,628
Other	(77)	(1,654)	4,211	(4,413)	1,659	(274)
Cash flows provided by (used in) investing activities	(77)	(23,997)	3,600	58,750	1,659	39,935
Cash flows from financing activities:						
Distributions	(43,950)	(43,950)	—	(5)	43,955	(43,950)
Long-term borrowings	—	34,000	—	—	—	34,000
Long-term debt repayments	—	(11,480)	—	—	—	(11,480)
Net intercompany borrowings (repayments)	3,048	91,657	(3,031)	(91,674)	—	—
Other	—	(3,060)	(221)	667	(1,659)	(4,273)
Cash flows provided by (used in) financing activities	(40,902)	67,167	(3,252)	(91,012)	42,296	(25,703)
Effect of foreign exchange rate changes on cash	—	—	—	(1,905)	—	(1,905)
Net increase (decrease) in cash and cash equivalents	—	61,486	(8)	7,901	—	69,379
Cash and cash equivalents at the beginning of the period	10	1,590	114	34,340	—	36,054
Cash and cash equivalents at the end of the period	$ 10	$ 63,076	$ 106	$ 42,241	$ —	$ 105,433

(a) Non-guarantor subsidiaries are wholly owned by Valero L.P., Valero Logistics or KPOP.

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

FORWARD-LOOKING STATEMENTS

This Form 10-Q contains certain estimates, predictions, projections, assumptions and other forward-looking statements that involve various risks and uncertainties. While these forward-looking statements, and any assumptions upon which they are based, are made in good faith and reflect our current judgment regarding the direction of our business, actual results will almost always vary, sometimes materially, from any estimates, predictions, projections, assumptions or other future performance suggested in this report. These forward-looking statements can generally be identified by the words "anticipates," "believes," "expects," "plans," "intends," "estimates," "forecasts," "budgets," "projects," "will," "could," "should," "may" and similar expressions. These statements reflect our current views with regard to future events and are subject to various risks, uncertainties and assumptions. Please read our Annual Report on Form 10-K for the year ended December 31, 2005, Part I, Item 1A "Risk Factors" for a discussion of certain of those risks, uncertainties and assumptions.

If one or more of these risks or uncertainties materialize, or if the underlying assumptions prove incorrect, our actual results may vary materially from those described in any forward-looking statement. Other unknown or unpredictable factors could also have material adverse effects on our future results. Readers are cautioned not to place undue reliance on this forward-looking information, which is as of the date of the Form 10-Q. We do not intend to update these statements unless it is required by the securities laws to do so, and we undertake no obligation to publicly release the result of any revisions to any such forward-looking statements that may be made to reflect events or circumstances after the date of this report or to reflect the occurrence of unanticipated events.

Overview

Valero L.P. is a publicly traded Delaware limited partnership formed in 1999 engaged in the crude oil and refined product transportation, terminalling and storage business. Valero L.P. has terminal facilities in the United States, the Netherlands Antilles, Canada, Mexico, the Netherlands and the United Kingdom.

We conduct our operations through our wholly owned subsidiaries, primarily Valero Logistics Operations, L.P. (Valero Logistics) and Kaneb Pipe Line Operating Partnership, L.P. (KPOP). Our operations are divided into four reportable business segments: refined product terminals, refined product pipelines, crude oil pipelines and crude oil storage tanks.

Refined Product Terminals. We own 57 terminals in the United States that provide storage and handling services on a fee basis for petroleum products, specialty chemicals and other liquids. We also own international terminal operations on the island of St. Eustatius, Netherlands Antilles, Point Tupper, Nova Scotia, in the United Kingdom, the Netherlands and in Nuevo Laredo, Mexico. We sold the eight terminals located in Australia and New Zealand on March 30, 2006.

Refined Product Pipelines. We own common carrier pipelines in Texas, Oklahoma, Colorado, New Mexico, Kansas, Nebraska, Iowa, South Dakota, North Dakota and Minnesota covering approximately 6,389 miles, consisting of the Central West System which is connected to Valero Energy refineries and the East Pipeline and the North Pipeline which we acquired from Kaneb. In addition, we own a 2,000 mile anhydrous ammonia pipeline located in Louisiana, Arkansas, Missouri, Illinois, Indiana, Iowa and Nebraska.

Crude Oil Pipelines. We own 797 miles of crude oil pipelines which transport crude oil and other feedstocks, such as gas oil, from various points in Texas, Oklahoma, Kansas and Colorado to Valero Energy's McKee, Three Rivers and Ardmore refineries as well as associated crude oil storage facilities in Texas and Oklahoma that are located along the crude oil pipelines. We also own 57 miles of crude oil pipeline in Illinois, which serves the ConocoPhillip's Wood River refinery.

Crude Oil Storage Tanks. We own 60 crude oil and intermediate feedstock storage tanks and related assets that store and deliver crude oil to Valero Energy's refineries in Benicia, Corpus Christi and Texas City.

We provide transportation, storage services and ancillary services to our customers, including Valero Energy, which indirectly owns our general partner. Factors that affect the results of our operations include:

- company-specific factors, such as integrity issues and maintenance requirements that impact the throughput rates of our assets;
- seasonal factors that affect the demand for refined products and fertilizers transported by and/or stored in our assets;
- industry factors, such as changes in the prices of petroleum products that affect demand and operations of our competitors; and
- other factors such as refinery utilization rates and maintenance turnaround schedules that impact the operations of refineries served by our assets.

Recent Developments

On January 15, 2006, UDS Logistics, LLC, an indirect, wholly owned subsidiary of Valero Energy, changed its name to Valero GP Holdings, LLC (Holdings). On January 25, 2006, Holdings formed Riverwalk Holdings, LLC, a Delaware limited liability company and a direct, wholly owned subsidiary, and contributed its 21.4% limited partnership interest (both common and subordinated units) in Valero L.P. and its 99.9% limited partnership interest in Riverwalk Logistics, L.P. to the newly formed subsidiary.

On March 31, 2006, Holdings filed a registration statement on Form S-1 with the Securities and Exchange Commission for an initial public offering of approximately 37% of its units representing limited liability company interests. All units will be sold by subsidiaries of Valero Energy, which initially will retain an approximate 63% ownership interest in Holdings, the principal owner of our general partner interest and the general partner incentive distribution rights and the owner of 21.4% limited partner interest in us. In the registration statement, Valero Energy states its intention to further reduce and ultimately sell all of its interest in Holdings pending market conditions.

On March 30, 2006, we sold our Australia and New Zealand subsidiaries to ANZ Terminals Pty. Ltd., for total proceeds of $65.0 million, plus working capital. The proceeds will be used for working capital purposes, including paying down outstanding debt. This transaction included the sale of eight terminals with an aggregate storage capacity of 1.1 million barrels. Revenues and pre-tax income related to the Australia and New Zealand subsidiaries, were included in loss from discontinued operations, and totaled $5.0 million and $0.6 million, respectively, for the three months ended March 31, 2006.

We purchased a 23.77% interest in Capwood pipeline from Valero Energy for approximately $13.0 million, which was paid from borrowings under our existing revolving credit agreement. The Capwood pipeline is a 57-mile crude oil pipeline that extends from Patoka, Illinois to Wood River, Illinois. Plains All American Pipeline L.P., the operator of the Capwood pipeline, owns the remaining 76.23% interest. Our financial statements include the results of operations of our interest in the Capwood pipeline in the crude oil pipelines segment for the three months ended March 31, 2006.

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Results of Operations

Three Months Ended March 31, 2006 Compared to Three Months Ended March 31, 2005

Financial Highlights
(Unaudited, Thousands of Dollars, Except Unit and Per Unit Data and Percentages)

	Three Months Ended March 31, 2006	Three Months Ended March 31, 2005	Change
Statement of Income Data:			
Revenues:			
Services revenues	147,929	56,635	91,294
Product sales	126,075	—	126,075
Total revenues	274,004	56,635	217,369
Costs and expenses:			
Cost of product sales	114,218	—	114,218
Operating expenses	71,070	19,685	51,385
General and administrative expenses	8,560	3,503	5,057
Depreciation and amortization	24,189	8,732	15,457
Total costs and expenses	218,037	31,920	186,117
Operating income	55,967	24,715	31,252
Equity income from joint ventures	1,206	378	828
Interest and other expenses, net	(15,465)	(5,829)	(9,636)
Income from continuing operations before income tax expense	41,708	19,264	22,444
Income tax expense	2,119	—	2,119
Income from continuing operations	39,589	19,264	20,325
Loss from discontinued operations	(138)	—	(138)
Net income	39,451	19,264	20,187
Less general partner's interest and incentive distributions	(4,199)	(1,476)	(2,723)
Limited partners' interest in net income	$ 35,252	$ 17,788	$ 17,464
Weighted-average units outstanding	46,809,749	23,041,394	
Net income per unit applicable to limited partners:			
Continuing operations	$ 0.75	$ 0.77	$ (0.02)
Discontinued operations	—	—	—
Net income	$ 0.75	$ 0.77	$ (0.02)

	March 31, 2006	December 31, 2005	
Balance Sheet Data:			
Long-term debt, including current portion	$ 1,188,228	$ 1,170,705	$ 17,523
Partners' equity	1,898,480	1,900,779	(2,299)
Debt-to-capitalization ratio (a)	38.5%	38.1%	0.4%

(a) Our debt-to-capitalization ratio is defined as our long-term debt, including current portion, divided by the sum of our long-term debt, including current portion, and partners' equity.

Segment Operating Highlights
(Thousands of Dollars, Except Barrels/Day Information)

	Three Months Ended March 31, 2006	2005	Change
Refined Product Terminals:			
Throughput (barrels/day)	252,275	253,531	(1,256)
Throughput revenues	$ 10,540	$ 9,937	$ 603
Storage lease revenues	59,533	—	59,533
Product sales (bunkering)	126,075	—	126,075
Total revenues	196,148	9,937	186,211
Cost of product sales	114,218	—	114,218
Operating expenses	43,979	4,497	39,482
Depreciation and amortization	10,906	1,859	9,047
Segment operating income	$ 27,045	$ 3,581	$ 23,464
Refined Product Pipelines:			
Throughput (barrels/day)	700,969	443,993	256,976
Revenues	$ 52,046	$ 22,182	$ 29,864
Operating expenses	19,802	9,303	10,499
Depreciation and amortization	10,139	3,857	6,282
Segment operating income	$ 22,105	$ 9,022	$ 13,083
Crude Oil Pipelines:			
Throughput (barrels/day)	427,675	381,086	46,589
Revenues	$ 14,049	$ 13,185	$ 864
Operating expenses	3,697	3,823	(126)
Depreciation and amortization	1,249	1,146	103
Segment operating income	$ 9,103	$ 8,216	$ 887
Crude Oil Storage Tanks:			
Throughput (barrels/day)	513,073	505,643	7,430
Revenues	$ 11,761	$ 11,331	$ 430
Operating expenses	3,592	2,062	1,530
Depreciation and amortization	1,895	1,870	25
Segment operating income	$ 6,274	$ 7,399	$ (1,125)
Consolidated Information:			
Revenues	$274,004	$ 56,635	$217,369
Cost of product sales	114,218	—	114,218
Operating expenses	71,070	19,685	51,385
Depreciation and amortization	24,189	8,732	15,457
Segment operating income	64,527	28,218	36,309
General and administrative expenses	8,560	3,503	5,057
Consolidated operating income	$ 55,967	$ 24,715	$ 31,252

Highlights

Net income for the three months ended March 31, 2006 increased $20.2 million compared to the three months ended March 31, 2005 due to higher consolidated segmental operating income, partially offset by increased general and administrative expense, increased interest expense and increased income tax expense. All of these increases predominantly resulted from the Kaneb Acquisition.

Consolidated segmental operating income for the three months ended March 31, 2006 increased $36.3 million compared to the three months ended March 31, 2005, primarily due to a $23.5 million increase in operating income for the refined product terminals segment and a $13.1 million increase in operating income for the refined product pipelines segment. These increases relate primarily to the effect of the Kaneb Acquisition. Except for storage lease revenues and bunker fuel sales, operating income for our segments depends upon the level of throughputs moving through our assets. In addition to the Kaneb Acquisition, which impacted only the refined product terminals and refined product pipelines segments, all of our segments are affected by scheduled maintenance turnarounds or other operational issues at refineries that we serve.

Refined Product Terminals

Revenues increased by $186.2 million for the three months ended March 31, 2006, compared to the three months ended March 31, 2005, primarily due to the Kaneb Acquisition, which contributed $126.1 million of bunkering revenues and $59.5 million of storage lease revenues.

Cost of product sales totaled $114.2 million for the three months ended March 31, 2006. Cost of product sales reflects the cost of bunker fuel sold to marine vessels at our facilities at St. Eustatius, Netherlands Antilles and Point Tupper, Nova Scotia, which we acquired as part of the Kaneb Acquisition.

Operating expenses increased $39.5 million for the three months ended March 31, 2006, compared to the three months ended March 31, 2005, primarily due to the inclusion of operating expenses related to the assets acquired in the Kaneb Acquisition. Operating expenses further increased compared to the three months ended March 31, 2005, due to increased regulatory and maintenance expense mainly related to the assets acquired with the Kaneb Acquisition and increased internal overhead expense resulting from increased headcount.

Depreciation and amortization expense increased $9.0 million for the three months ended March 31, 2006, compared to the three months ended March 31, 2005, primarily due to an increase in our property and equipment related to the Kaneb Acquisition.

Refined Product Pipelines

Revenues increased by $29.9 million for the three months ended March 31, 2006, compared to the three months ended March 31, 2005, primarily due to the Kaneb Acquisition, which increased throughputs by 218,394 barrels per day, resulting in additional revenues of $27.2 million. Revenues also increased due to the expansion of a refined product pipeline in South Texas, which commenced operations on the Edinburg to Harlingen segment in October 2005, and the Harlingen to Brownsville segment in March 2006. In addition, revenues increased due to increased volumes in the Dos Laredos pipeline system.

Operating expenses increased by $10.5 million for the three months ended March 31, 2006, compared to the three months ended March 31, 2005, primarily due to the inclusion of operating expenses of $11.2 million related to the assets acquired in the Kaneb Acquisition. Partially offsetting the increase in operating expenses was a decrease in power costs due to our power optimization program and decreased environmental expenses.

Depreciation and amortization expense increased by $6.3 million for the three months ended March 31, 2006 compared to the three months ended March 31, 2005, primarily due to increases in our property and equipment related to the Kaneb Acquisition.

Crude Oil Pipelines

Revenues increased by $0.9 million for the three months ended March 31, 2006, compared to the three months ended March 31, 2005, primarily from our purchase of the Capwood pipeline, which increased throughputs by 45,859 barrels per day, resulting in additional revenues of $0.5 million. Revenues also increased on the Ringgold to Wasson crude oil pipeline, despite lower overall throughputs to the Ardmore refinery, as throughputs increased in this higher tariff rate pipeline.

Crude Oil Storage Tanks

Revenues increased by $0.4 million for the three months ended March 31, 2006, compared to the three months ended March 31, 2005, primarily due to increased throughput in our Corpus Christi crude oil storage tanks.

Operating expenses increased by $1.5 million for the three months ended March 31, 2006, compared to the three months ended March 31, 2005, due to higher maintenance expense on the Corpus Christi and Texas City crude oil storage tanks.

General

General and administrative expenses increased by $5.1 million for the three months ended March 31, 2006, compared to the three months ended March 31, 2005, primarily due to increased headcount as a result of the Kaneb Acquisition.

Interest expense increased by $9.9 million for the three months ended March 31, 2006, compared to the three months ended March 31, 2005, due to higher average debt balances resulting from debt assumed in the Kaneb Acquisition and debt incurred to fund the Kaneb Acquisition combined with higher interest rates in 2006.

Income tax expense was $2.1 million for the three months ended March 31, 2006, all of which related to certain operations acquired in the Kaneb Acquisition that are conducted through separate taxable wholly owned corporate subsidiaries.

Outlook

We expect certain refineries that we serve to experience increased turnaround activity in the second and third quarters of 2006. We expect this increased level of turnaround activity to negatively impact our earnings by approximately $3.6 million. Despite the turnaround activity in the third quarter, we expect overall earnings for the second half of 2006 to increase compared to the first half of the year primarily due to increases in pipeline tariffs, which go into effect on July 1, 2006, and higher throughput volumes from our strategic growth projects.

LIQUIDITY AND CAPITAL RESOURCES

General

Our primary cash requirements are for distributions to partners, debt service, reliability and expansion capital expenditures, acquisitions and normal operating expenses. We have typically generated sufficient cash from our current operations to fund day-to-day operating and general and administrative expenses, reliability capital expenditures and distribution requirements. We also have available borrowing capacity under our existing revolving credit facility and, to the extent necessary, may raise additional funds through equity or debt offerings under our $750 million universal shelf registration statement to fund strategic capital expenditures or other cash requirements not funded from operations. However, there can be no assurance regarding the availability of any additional funds or whether such additional funds can be obtained on terms acceptable to us.

Cash Flows for the Three Months Ended March 31, 2006 and 2005

Net cash provided by operating activities for the three months ended March 31, 2006 was $57.1 million compared to $15.3 million for the three months ended March 31, 2005. The increase in cash generated from operating activities is primarily due to higher net income and depreciation expense resulting from the Kaneb Acquisition.

Net cash provided by operating activities for the three months ended March 31, 2006, combined with available cash on hand, was used to fund distributions to unitholders and the general partner in the amount of $44.0 million. The proceeds from long-term debt borrowings totaling $34.0 million were used to fund the purchase of the Capwood pipeline and capital expenditures. The proceeds from the sale of the Australia and New Zealand subsidiaries totaling $68.6 million increased our cash balance as of March 31, 2006.

Net cash provided by operating activities for the three months ended March 31, 2005 was $15.3 million. The net cash provided by operations, combined with available cash on hand, was used primarily to fund distributions to unitholders and the general partner in the amount of $19.9 million. Additionally, we used cash from those sources in combination with long-term debt borrowings totaling $4.0 million to fund $4.3 million of capital expenditures and pre-acquisition costs associated with the Kaneb Acquisition totaling $2.0 million.

Partners' Equity

Cash Distributions. On January 27, 2006, we declared a quarterly cash distribution of $0.855 per unit paid on February 14, 2006 to unitholders of record on February 7, 2006, which totaled $44.0 million. On April 18, 2006, we declared a quarterly cash distribution of $0.885 per unit to be paid on May 12, 2006 to unitholders of record on May 5, 2006, which totaled $45.8 million.

The following table reflects the allocation of total cash distributions to the general and limited partners applicable to the period in which the distributions were earned:

	Three Months Ended March 31,	
	2006	2005
	(Thousands of Dollars, Except Per Unit Data)	
General partner interest	$ 916	$ 399
General partner incentive distribution	3,480	1,112
Total general partner distribution	4,396	1,511
Limited partners' distribution	41,427	18,433
Total cash distributions	$45,823	$19,944
Cash distributions per unit applicable to limited partners	$ 0.885	$ 0.800

Subordinated Units. We satisfied all the conditions included in our partnership agreement for the subordination period to end. Accordingly, the subordination period ended effective April 1, 2006 and all 9,599,322 subordinated units converted into common units on a one-for-one basis on May 8, 2006, the first business day after the record date for the distribution related to the first quarter earnings of 2006. Riverwalk Holdings, LLC held the 9,599,322 subordinated units at the time of conversion.

Capital Requirements

The petroleum pipeline and terminalling industry is capital-intensive, requiring significant investments to maintain, upgrade or enhance existing operations and to comply with environmental and safety laws and regulations.

Our capital expenditures consist primarily of:

- reliability capital expenditures, such as those required to maintain equipment reliability and safety and to address environmental and safety regulations; and
- expansion capital expenditures, such as those to expand and upgrade pipeline capacity and to construct new pipelines, terminals and storage tanks. In addition, expansion capital expenditures may include acquisitions of pipelines, terminals, storage tank assets, or other logistic assets.

During the three months ended March 31, 2006, we incurred reliability capital expenditures of $6.2 million primarily related to the upgrade and enhancement of the assets acquired with the Kaneb Acquisition. Expansion capital expenditures of $9.4 million during the three months ended March 31, 2006 were primarily related to the pipeline project to construct approximately 110 miles of new pipeline in the northeastern Mexico and South Texas regions, which we expect to complete by July 1, 2006.

For 2006, we expect to incur approximately $136.0 million of capital expenditures, including $47.0 million for reliability capital projects and $89.0 million for expansion capital projects. We continuously evaluate our capital forecast and make changes as economic conditions warrant. If conditions warrant, our actual capital expenditures for 2006 may exceed the forecasted amounts. We believe cash generated from operations combined with other sources of liquidity previously described will be sufficient to fund our capital expenditures in 2006.

Other Contingencies

We are subject to certain loss contingencies, the outcome of which could have an effect on our cash flows. Specifically, we may be required to make substantial payments to the U.S. Department of Justice for certain remediation costs as further disclosed in Note 5 of Condensed Notes to Consolidated Financial Statements.

Long-Term Contractual Obligations

$400 Million Revolving Credit Agreement. During the three months ended March 31, 2006, we borrowed $34.0 million under our $400 million 2005 revolving credit agreement (the 2005 Revolving Credit Agreement) to fund the purchase of the Capwood pipeline and our capital expenditures. Additionally, we repaid $11.0 million during the three months ended March 31, 2006. The 2005 Revolving Credit Agreement bears interest based on either an alternative base rate or LIBOR, which was 5.5% as of March 31, 2006. As of March 31, 2006, we had $372.1 million available for borrowing under our 2005 Revolving Credit Agreement.

Interest Rate Swaps. As of March 31, 2006, the weighted-average interest rate for our interest rate swaps was 7.1%. As of March 31, 2006 and December 31, 2005, the aggregate estimated fair value of the interest rate swaps included in other long-term liabilities in our consolidated balance sheets was $7.9 million and $4.0 million, respectively.

Other

In Holding's registration statement on Form S-1, Valero Energy stated its intention to ultimately sell of its interest in Holdings pending market conditions. If Valero Energy ultimately sells all of its interests in Holdings, it will no longer own our general partner, which would trigger certain requirements in our debt instruments. As a result, we took the following actions:

- On April 19, 2006, Valero Logistics commenced a consent solicitation from the holders of its $100.0 million 6.875% senior notes due 2012 and its $250.0 million 6.05% senior notes due 2013 in order to amend the change of control covenant requiring that Valero Energy or an investment grade entity own 51% of our general partner interests as set forth in the indenture governing the notes of both such series. Holders of record as of April 18, 2006 who consent to the proposed amendment will receive $5.00 per $1,000 principal amount with respect to 6.05% Senior Notes and $2.50 per $1,000 principal amount with respect to the 6.875% senior notes. The consent solicitation will expire on May 10, 2006, unless further extended.
- In May 2006, we initiated discussions to amend the 2005 Revolving Credit Agreement, the $525 Term Loan Agreement and the UK Term Loan in order to eliminate the change in control provision requiring Valero Energy to own at least a majority of the outstanding equity interests in our general partner.

Environmental, Health and Safety

We are subject to extensive federal, state and local environmental and safety laws and regulations, including those relating to the discharge of materials into the environment, waste management, pollution prevention measures, pipeline integrity and operator qualifications, among others. Because environmental and safety laws and regulations are becoming more complex and stringent and new environmental and safety laws and regulations are continuously being enacted or proposed, the level of future expenditures required for environmental, health and safety matters is expected to increase.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

The following table provides information about our long-term debt and interest rate derivative instruments, all of which are sensitive to changes in interest rates. For long-term debt, principal cash flows and related weighted-average interest rates by expected maturity dates are presented. For interest rate swaps, the table presents notional amounts and weighted-average interest rates by expected (contractual) maturity dates. Weighted-average variable rates are based on implied forward interest rates in the yield curve at the reporting date.

	March 31, 2006							
	Expected Maturity Dates							
	2006	2007	2008	2009	2010	Thereafter	Total	Fair Value
	(Thousands of Dollars, Except Interest Rates)							
Long-term Debt:								
Fixed rate	$ 566	$611	$660	$713	$ 37,239	$854,881	$894,670	$926,685
Average interest rate	8.0%	8.0%	8.0%	8.0%	6.7%	6.6%	6.6%	
Variable rate	$ —	$—	$—	$—	$252,000	$ —	$252,000	$252,000
Average interest rate	—	—	—	—	5.6%	—	5.6%	
Interest Rate Swaps Fixed to Variable:								
Notional amount	$ —	$—	$—	$—	$ —	$167,500	$167,500	$ (7,910)
Average pay rate	7.1%	7.0%	7.0%	7.0%	7.1%	7.1%	7.1%	
Average receive rate	6.3%	6.3%	6.3%	6.3%	6.3%	6.3%	6.3%	

	December 31, 2005							
	Expected Maturity Dates							
	2006	2007	2008	2009	2010	Thereafter	Total	Fair Value
	(Thousands of Dollars, Except Interest Rates)							
Long-term Debt:								
Fixed rate	$1,046	$611	$660	$713	$ 36,901	$854,881	$894,812	$954,039
Average interest rate	8.0%	8.0%	8.0%	8.0%	6.7%	6.6%	6.6%	
Variable rate	$ —	$—	$—	$—	$229,000	$ —	$229,000	$229,000
Average interest rate	—	—	—	—	5.2%	—	5.2%	
Interest Rate Swaps Fixed to Variable:								
Notional amount	$ —	$—	$—	$—	$ —	$167,500	$167,500	$ (4,002)
Average pay rate	6.6%	6.6%	6.6%	6.6%	6.7%	6.6%	6.6%	
Average receive rate	6.3%	6.3%	6.3%	6.3%	6.3%	6.3%	6.3%	

Item 4. Controls and Procedures

(a) *Evaluation of disclosure controls and procedures.*

Our management has evaluated, with the participation of the principal executive officer and principal financial officer of Valero GP, LLC, the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934) as of the end of the period covered by this report, and has concluded that our disclosure controls and procedures were effective as of March 31, 2006.

(b) *Changes in internal control over financial reporting.*

There has been no change in our internal control over financial reporting that occurred during our last fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

Port of Vancouver Matter. We own a chemical and refined products terminal on property owned by the Port of Vancouver, and we lease the land under the terminal from the Port of Vancouver. Under an Agreed Order entered into with the Washington Department of Ecology when Kaneb purchased the terminal in 1998, Kaneb agreed to investigate and remediate groundwater contamination by the terminal's previous owner and operator originating from the terminal. Investigation and remediation at the terminal are ongoing, in compliance with the Agreed Order. In April 2006, the Washington Department of Ecology commented on our site investigation work plan and asserted that the groundwater contamination at the terminal was commingled with a groundwater contamination plume under other property owned by the Port of Vancouver. We dispute this assertion. No lawsuits have been filed against us in this matter, and our liability for any portion of total future remediation costs of the commingled plume is not reasonably estimable at this time. Factors that could affect estimated remediation costs include whether Kaneb will be found to have ultimate responsibility for some portion of the commingled plume, the Port of Vancouver's contribution to the remediation effort and the amount the Port of Vancouver actually receives from other potentially responsible parties.

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

(a) **Unregistered Sales of Equity Securities.** None.

(b) **Use of Proceeds.** Not applicable.

(c) **Issuer Purchases of Equity Securities.** The following table discloses purchases of Valero L.P.'s common units made by Valero GP, LLC for the periods shown below.

Period	Total Number of Units Purchased (1)	Average Price Paid per Unit	Total Number of Units Purchased as a Part of Publicly Announced Plans or Programs	Maximum Number (or Approximate Dollar Value) of Units that May Yet Be Purchased Under the Plans or Programs
January 2006	0	n/a	n/a	n/a
February 2006	22,000	$ 51.22	n/a	n/a
March 2006	10,000	$ 50.63	n/a	n/a
Total	32,000	$ 51.03	n/a	n/a

(1) The units reported in this column represent purchases that were settled in the first quarter of 2006 relating to Valero GP, LLC's purchases of Valero L.P. units in open-market transactions to meet its obligations under Valero GP, LLC employee benefit plans. None of the reported units were purchased through any publicly announced unit purchase plan or program.

Item 6. Exhibits

*Exhibit 10.01	Third Amended and Restated Services Agreement among Diamond Shamrock Refining and Marketing Company, Valero Corporate Services Company, Valero L.P., Valero Logistics Operations, L.P., Riverwalk Logistics, L.P. and Valero GP, LLC, dated as of January 1, 2006
*Exhibit 10.02	Memorandum of Understanding Regarding Office Lease Agreement between Valero Corporate Services Company as Landlord, and Valero Logistics Operations L.P. as Tenant, effective as of January 1, 2006.
*Exhibit 12.01	Statement of Computation of Ratio of Earnings to Fixed Charges
*Exhibit 31.01	Rule 13a-14(a) Certifications (under Section 302 of the Sarbanes-Oxley Act of 2002)
*Exhibit 32.01	Section 1350 Certifications (as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002)

* Filed herewith.

Table of Contents

SIGNATURES

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

VALERO L.P.
(Registrant)

By: Riverwalk Logistics, L.P., its general partner
By: Valero GP, LLC, its general partner

By: /s/ Curtis V. Anastasio
Curtis V. Anastasio
President and Chief Executive Officer
May 9, 2006

By: /s/ Steven A. Blank
Steven A. Blank
Senior Vice President, Chief Financial Officer and Treasurer
May 9, 2006

By: /s/ Thomas R. Shoaf
Thomas R. Shoaf
Vice President and Controller
May 9, 2006

Exhibit 10.01

THIRD AMENDED AND RESTATED

SERVICES AGREEMENT

AMONG

DIAMOND SHAMROCK REFINING AND MARKETING COMPANY

VALERO CORPORATE SERVICES COMPANY

VALERO L.P.

VALERO LOGISTICS OPERATIONS, L.P.

RIVERWALK LOGISTICS, L.P.

AND

VALERO GP, L.L.C.

DATED AS OF JANUARY 1, 2006

THIRD AMENDED AND RESTATED SERVICES AGREEMENT

This THIRD AMENDED AND RESTATED SERVICES AGREEMENT (this "Agreement") is entered into effective as of January 1, 2006 (the "Effective Date") by and among DIAMOND SHAMROCK REFINING AND MARKETING COMPANY, a Delaware corporation ("DSRMC") and VALERO CORPORATE SERVICES COMPANY, a Delaware corporation ("VSCS"), both indirect wholly owned subsidiaries of Valero Energy Corporation ("Valero Energy"), VALERO L.P., a publicly traded Delaware limited partnership (the "Partnership"), VALERO LOGISTICS OPERATIONS, L.P. (the "Operating Partnership"), a Delaware limited partnership and an indirect wholly owned subsidiary of the Partnership, RIVERWALK LOGISTICS, L.P., the general partner (the "General Partner") of the Partnership, and its general partner, VALERO GP, LLC ("Valero GP").

RECITALS

WHEREAS, certain parties hereto entered into a Services Agreement effective July 1, 2000 pursuant to which DSRMC agreed to provide certain corporate, general and administrative services to the General Partner in exchange for an administrative services fee; and

WHEREAS, the Services Agreement was amended and restated (the "First Amended and Restated Services Agreement") effective April 1, 2004; and

WHEREAS, on July 1, 2005, the Partnership completed its acquisition of Kaneb Services, LLC and Kaneb Pipe Line Partners, L.P., effectively doubling the Partnership's operations; and

WHEREAS, the Services Agreement was amended and restated as of July 1, 2005 (the "Second Amended and Restated Services Agreement") to reflect the significant changes in operations that resulted from the acquisition; and

WHEREAS, management of the General Partner has determined that some of the services currently being provided by affiliates of Valero Energy under the Second Amended and Restated Services Agreement should be performed by the Partnership Parties and has determined that the Second Amended and Restated Services Agreement should be further amended to more accurately reflect the provision of the corporate, general and administrative services;

WHEREAS, on January 26, 2006, upon recommendation by management of the General Partner and the Conflicts Committee of the Board of Directors of the General Partner, the Board of Directors of the General Partner approved the terms of this Agreement; and

WHEREAS, VCSC, for itself and its Affiliates, has agreed to provide certain administrative services under this Agreement to Valero GP, the General Partner, the Partnership and the Operating Partnership (individually, a "Partnership Party," and collectively, the "Partnership Parties"); and

NOW, THEREFORE, for and in consideration of the mutual covenants contained in this Agreement, the parties hereto hereby agree to amend and restate the Amended and Restated Services Agreement as follows:

ARTICLE I
PROVISION OF SERVICES

Section 1.1 Provision of Administrative Services by VCSC and its Affiliates.

(a) Administrative Services. VCSC or any Affiliate or designee of VCSC shall provide to the Partnership Parties certain non-exclusive management, employee-related and other services as set forth on Exhibit A hereto, and such other services as VCSC and Valero GP may from time to time agree (the "Administrative Services").

For purposes of this Agreement, "Affiliates" means entities that directly or indirectly through one or more intermediaries control, or are controlled by, or are under common control with, such party, and the term "control" shall mean the possession, directly or indirectly, of the power to direct or cause the direction of management and policies of an entity, whether through the ownership of voting securities, by contract or otherwise, provided, however, that with respect to VCSC or Valero Energy, the term "Affiliate" shall exclude Valero GP Holdings, LLC, Valero GP, the General Partner, the Partnership and the Operating Partnership.

(b) Telecommunications Services. VCSC or any Affiliate of VCSC shall provide the Partnership Parties with Telecommunication Services substantially similar to those provided to Affiliates of VCSC during the term of this Agreement. Telecommunications Services shall include costs of circuits related to telecommunications hardware, cell phones, Blackberries (or their functional equivalent) and other personal communications devices, and local and long distance carrier service.

(c) Additional Services. VCSC or any Affiliate of VCSC shall provide the Partnership Parties with such other services as Valero GP may request from time to time during the term of this Agreement and for such additional compensation as the parties may agree.

(d) Direct Charges. Notwithstanding Section 1.1 (a) above, the following items will be directly charged to the Partnership ("Direct Charges"):

all third party expenses directly related to the Partnership Parties, including, but not limited to, public company costs, outside legal fees, outside accounting fees, fees and expenses of external advisors and consultants, and insurance costs, including but not limited to, general liability, automobile liability, comprehensive liability, excess liability, property and directors and officers.

(d) Nature and Quality of Services. The quality of the Administrative Services and the Telecommunications Services shall be substantially identical to those provided to other subsidiaries and Affiliates of VCSC.

Section 1.2 Fees for Administrative Services.

(a) Commencing on the Effective Date of this Agreement, and for each contract year thereafter, the Partnership shall pay to VCSC an annual fee (the "Administrative Services Fee"). The Administrative Services Fee for the contract year ended December 31, 2006 shall be $765,000, for the contract year ended December 31, 2007 shall be $1.765 million, and thereafter such fee shall be $2.265 million for the contract year ended December 31, 2008 and the years following, subject to adjustment as provided in paragraph (b) below.

(b) On the last day of each contract year starting with the contract year ending December 31, 2006, and prior to the beginning of the next contract year, the Administrative Services Fee shall be increased by an amount equal to Valero Energy's general annual merit increase percentage for the just completed contract year.

(c) The General Partner, with the approval and consent of the Conflicts Committee, may agree on behalf of the Partnership to further modifications in the Administrative Services Fee in connection with changed levels of Administrative Services provided to the Partnership Parties due to expansions of the Partnership's operations through acquisition or construction of new assets or businesses.

(d) At the end of each contract year, the scope of the Administrative Services and the related Administrative Services Fee are subject to review either at the request of VCSC or the Partnership Parties, in either case by providing 10 days written notice to the other party but in no event later than 60 days before the end of the applicable contract year, with such review to be completed no later than March 31 of the immediately following contract year, with any modification of the Administrative Services Fee other than as provided in paragraphs (a) and (b) above subject to the consent and approval of the Conflicts Committee.

(e) Any fees payable hereunder for periods less than a full contract year shall be prorated for the period services were provided based on the actual number of days elapsed and a year of 365 days.

(f) The Partnership shall pay all applicable sales taxes on the portion of the Administrative Services Fee attributable to IS Support.

Section 1.3 Fees for Telecommunications Services.

Commencing on the Effective Date of this Agreement, and for each contract year thereafter, the Partnership shall pay to VCSC an annual fee for the provision of the Telecommunications Services (the "Telecommunications Fee"). The Telecommunications Fee for the contract year ending December 31, 2006 shall be $1.1 million.

(b) (i) The Telecommunications Fee will automatically escalate on the first anniversary date of this Agreement by the percentage increase in the Consumer Price Index for All Urban Consumers ("CPI-U") as published by the U.S. Department of Labor, Bureau of Labor Statistics. The percentage increase in the CPI-U means the average percentage increase in the CPI-U over the first twelve (12) of the fifteen (15) months preceding the escalation date.

(ii) On the second anniversary of this Agreement and thereafter, the Telecommunications Fee shall be adjusted annually to reflect VCSC's actual cost to provide the Telecommunications Services.

(c) At the end of each contract year, the scope of the Telecommunications Services and the related Telecommunications Fee are subject to review either at the request of VCSC or the Partnership Parties, in either case by providing 10 days written notice to the other party but in no event later than 60 days before the end of the applicable contract year, with such review to be completed no later than March 31 of the immediately following contract year, with any modification of the Telecommunications Fee other than as provided in paragraphs (a) and (b) above subject to the consent and approval of the Conflicts Committee.

(d) Any fees payable hereunder for periods less than a full contract year shall be prorated for the period services were provided based on the actual number of days elapsed and a year of 365 days.

Section 1.3 Payment of Fees.

(a) The fees to be paid pursuant to this Agreement shall be paid by the Partnership in equal monthly installments in arrears within 30 days of the end of the month.

(b) To the extent reasonably practicable, all third party invoices for Direct Charges shall be submitted to the Partnership Parties, for payment. For Direct Charges not paid directly by the Partnership Parties, if any, VCSC shall present Valero GP with an invoice within 10 days after the end of each calendar month which reflects an amount equal to all Direct Charges reimbursable to VCSC. The Partnership shall pay such sum within 30 days of the end of the applicable calendar month.

Section 1.4 Cancellation or Reduction of Services. The Partnership Parties may terminate or reduce the level of any Administrative or Telecommunications Service on 60 days' prior written notice to VCSC. Upon such termination or reduction, the Administrative Services Fee or the Telecommunications Fee shall be reduced accordingly, whether on a temporary or a permanent basis, for such time as such service is reduced or terminated.

Section 1.5. Term. The provisions of this Article I will apply until this Agreement is terminated or amended in accordance with Section 2.1 or Section 2.13, respectively.

ARTICLE II
MISCELLANEOUS

Section 2.1 Termination.

(a) This Agreement shall terminate on December 30, 2010 (the "Initial Term"); provided that this Agreement shall automatically continue for successive two year terms after the Initial Term unless or until one year's advance notice is given by VCSC to terminate this Agreement, in which case this Agreement shall terminate one year after such notice is delivered. Notwithstanding the foregoing, any Partnership Party (a) may terminate the provision of one or more Administrative Services, reduce the level of one or more Administrative Services in accordance with the provisions of Section 1.4 hereof or terminate or reduce the level of Telecommunications Services provided hereunder, and (b) shall have the right at any time to terminate this Agreement by giving written notice to VCSC, and in such event this Agreement shall terminate one hundred and eighty (180) days from the date on which such notice is given.

(b) Notwithstanding Section 2.1(a), if a Change of Control (as defined below) of Valero GP Holdings, LLC ("Holdings") or Valero GP occurs, this Agreement shall terminate. The following shall constitute a Change of Control:

(i) Holdings shall cease to own, directly or indirectly, 100% of each of Valero GP and the General Partner;

(ii) both (A) the Valero Energy Affiliates (as defined below) shall be in the aggregate the legal or beneficial owners (within the meaning of Rule 13d-3 under the Securities Exchange Act of 1934, as amended) of less than a majority of the combined voting power of the then total membership interests (including all securities which are convertible into membership interests) of Holdings, and (B) any Person (as defined below) or Group of Persons (as defined below) acting in concert as a partnership or other Group (a "Group of Persons"), other than one or more of the Valero Energy Affiliates, shall be the legal or beneficial owner (within the meaning of Rule 13d-3 under the Securities Exchange Act of 1934, as amended) of 20% or more of the combined voting power of the then total membership interests (including all securities which are convertible into membership interests) of Holdings, provided, that a "Group of Persons" shall not include the underwriter in any firm underwriting undertaken in connection with the initial public offering or any subsequent public offering of Holdings; or

(iii) occupation of a majority of the seats (other than vacant seats) on the Board of Directors (or Board of Managers) of Holdings by Persons who were neither (A) nominated by the board of directors of Holdings nor (B) appointed by directors, a majority of whom were so nominated.

(c) For purposes of Section 2.1 (b) the following terms shall mean:

"*Associate*" means, when used to indicate a relationship with any Person, (a) any corporation or organization which such Person is a director, officer or partner or is, directly or indirectly, the owner of 20% or more of any class of voting stock or other voting interest; (b) any trust or other estate in which such Person has at least a 20% beneficial interest or as to which such Person serves as trustee or in a similar fiduciary capacity; and (c) any relative or spouse of such Person, or any relative of such spouse, who has the same principal residence as such Person.

"Group" means a Person that with our through any of its Affiliates or Associates has any agreement, arrangement or understanding for the purpose of acquiring, holding, voting (except voting pursuant to a revocable proxy or consent given to such Person in response to a proxy or consent solicitation made to ten or more Persons), exercising investment power or disposing of any membership interests of Holdings with any other Person that beneficially owns, or whose Affiliates or Associates beneficially own, directly or indirectly, membership interests of Holdings.

"*Person*" means an individual or a corporation, limited liability company, partnership, joint venture, trust, unincorporated organization or other enterprise (including an employee benefit plan), association, government agency or political subdivision thereof or other entity.

"Valero Energy Affiliates" shall mean any and all Affiliates of Valero Energy.

Section 2.2 No Third Party Beneficiary. The provisions of this Agreement are enforceable solely by the parties to the Agreement and no limited partner, assignee or other person shall have the right, separate and apart from the parties hereto, to enforce any provisions of this Agreement or to compel an party to this Agreement to comply with the terms of this Agreement.

Section 2.3 No Fiduciary Duties The parties hereto shall not have any fiduciary obligations or duties to the other parties by reason of this Agreement. Subject to the Omnibus Agreement among Valero Energy (as successor to Ultramar Diamond Shamrock Corporation), Valero GP, the General Partner, the Partnership and Valero Logistics Operations, L.P., dated as of April 16, 2001, as such agreement may be amended from time to time, any party hereto may conduct any activity or business for its own profit whether or not such activity or business is in competition with any activity or business of the other party.

Section 2.4 Limited Warranty; Limitation of Liability

VCSC represents that it will provide or cause the services to be provided to the Partnership Parties with reasonable care and in accordance with all applicable laws, rules, and regulations, including without limitation those of the Federal Energy Regulatory Commission. EXCEPT AS SET FORTH IN THE IMMEDIATELY PRECEDING SENTENCE AND IN SECTION 1.1 (d), ALL PRODUCTS OBTAINED FOR THE PARTNERSHIP PARTIES ARE AS IS, WHERE IS, WITH ALL FAULTS AND VCSC MAKES NO (AND HEREBY DISCLAIMS AND NEGATES ANY AND ALL) REPRESENTATIONS AND WARRANTIES, EXPRESS OR IMPLIED, INCLUDING THE WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE WITH RESPECT TO THE SERVICES RENDERED OR PRODUCTS OBTAINED FOR THE PARTNERSHIP PARTIES. FURTHERMORE, THE PARTNERSHIP PARTIES MAY NOT RELY UPON ANY REPRESENTATION OR WARRANTY, EXPRESS OR IMPLIED, INCLUDING THE WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE MADE TO VCSC BY ANY PARTY (INCLUDING, AN AFFILIATE OF VCSC) PERFORMING SERVICES ON BEHALF OF VCSC HEREUNDER, UNLESS SUCH PARTY MAKES AN EXPRESS WARRANTY TO VALERO GP OR THE PARTNERSHIP PARTIES. HOWEVER, IN THE CASE OF SERVICES PROVIDED BY A THIRD PARTY FOR THE PARTNERSHIP PARTIES, IF THE THIRD PARTY PROVIDER OF SUCH SERVICES MAKES AN EXPRESS WARRANTY TO ANY OF THE PARTNERSHIP PARTIES, THE PARTNERSHIP PARTIES ARE ENTITLED TO CAUSE VCSC TO RELY ON AND TO ENFORCE SUCH WARRANTY.

IT IS EXPRESSLY UNDERSTOOD BY THE PARTNERSHIP PARTIES THAT VCSC AND ITS AFFILIATES SHALL HAVE NO LIABILITY FOR THE FAILURE OF THIRD PARTY PROVIDERS TO PERFORM ANY SERVICES HEREUNDER AND FURTHER THAT VCSC AND ITS AFFILIATES SHALL HAVE NO LIABILITY WHATSOEVER FOR THE SERVICES PROVIDED BY ANY SUCH THIRD PARTY UNLESS IN EITHER EVENT SUCH SERVICES ARE PROVIDED IN A MANNER WHICH WOULD EVIDENCE GROSS NEGLIGENCE OR INTENTIONAL MISCONDUCT ON THE PART OF VCSC OR ITS AFFILIATES BUT VCSC SHALL, ON BEHALF OF THE PARTNERSHIP PARTIES, PURSUE ALL RIGHTS AND REMEDIES UNDER ANY SUCH THIRD PARTY CONTRACT. THE PARTNERSHIP PARTIES AGREE THAT THE REMUNERATION PAID TO VCSC HEREUNDER FOR THE SERVICES TO BE PERFORMED REFLECT THIS LIMITATION OF LIABILITY AND DISCLAIMER OF WARRANTIES. IN NO EVENT SHALL VCSC BE LIABLE TO THE PARTNERSHIP PARTIES OR ANY OTHER PERSON FOR ANY INDIRECT, SPECIAL, OR CONSEQUENTIAL DAMAGES RESULTING FROM ANY ERROR IN THE PERFORMANCE OF SERVICES OR FROM THE BREACH OF THIS AGREEMENT, REGARDLESS OF THE FAULT OF VCSC, ANY VCSC AFFILIATE, OR ANY THIRD PARTY PROVIDER OR WHETHER VCSC, ANY VCSC AFFILIATE, OR THE THIRD PARTY PROVIDER ARE WHOLLY, CONCURRENTLY, PARTIALLY, OR SOLELY NEGLIGENT. TO THE EXTENT ANY THIRD PARTY PROVIDER HAS LIMITED ITS LIABILITY TO VCSC OR ITS AFFILIATE FOR SERVICES UNDER AN OUTSOURCING OR OTHER AGREEMENT, THE PARTNERSHIP PARTIES AGREE TO BE BOUND BY SUCH LIMITATION OF LIABILITY FOR ANY PRODUCT OR SERVICE PROVIDED TO THE PARTNERSHIP PARTIES BY SUCH THIRD PARTY PROVIDER UNDER VCSC'S OR SUCH AFFILIATE'S AGREEMENT.

Section 2.5 Force Majeure. If any party to this Agreement is rendered unable by force majeure to carry out its obligations under this Agreement, other than a party's obligation to make payments as provided for herein, that party shall give the other parties prompt written notice of the force majeure with reasonably full particulars concerning it. Thereupon, the obligations of the party giving the notice, insofar as they are affected by the force majeure, shall be suspended during, but no longer than the continuance of, the force majeure. The affected party shall use all reasonable diligence to remove or remedy the force majeure situation as quickly as practicable.

The requirement that any force majeure situation be removed or remedied with all reasonable diligence shall not require the settlement of strikes, lockouts or other labour difficulty by the party involved, contrary to its wishes. Rather, all such difficulties may be handled entirely within the discretion of the party concerned.

The term "force majeure" means any one or more of: (a) an act of God, (b) a strike, lockout, labour difficulty or other industrial disturbance, (c) an act of a public enemy, war, blockade, insurrection or public riot, (d) lightning, fire, storm, flood or explosion, (e) governmental action, delay, restraint or inaction, (f) judicial order or injunction, (g) material shortage or unavailability of equipment, or (h) any other cause or event, whether of the kind specifically enumerated above or otherwise, which is not reasonably within the control of the party claiming suspension.

Section 2.6 Further Assurances. In connection with this Agreement and all transactions contemplated by this Agreement, each signatory party hereto agrees to execute and deliver such additional documents and instruments as may be required for a party to provide the services hereunder and to perform such other additional acts as may be necessary or appropriate to effectuate, carry out, and perform all of the terms and provisions of this Agreement.

Section 2.7 Time of the Essence. Time is of the essence in this Agreement.

Section 2.8 Notices. Any notice, request, demand, direction or other communication required or permitted to be given or made under this Agreement to a party shall be in writing and may be given by hand delivery, postage prepaid first-class mail delivery, delivery by a reputable international courier service guaranteeing next business day delivery or by facsimile (if confirmed by one of the foregoing methods) to such party at its address noted below:

(a) in the case of VCSC, to:

Valero Corporate Services Company
One Valero Way
San Antonio, Texas 78249
Attention: Legal Department
Telecopy: (210) 345-5889

(b) in the case of the General Partner and Valero GP, to:

Valero GP, LLC
One Valero Way
San Antonio, Texas 78249
Attention: Legal Department
Telecopy: (210) 345-4861

or at such other address of which notice may have been given by such party in accordance with the provisions of this Section.

Section 2.9 Counterparts. This Agreement may be executed in several counterparts, no one of which needs to be executed by all of the parties. Such counterpart, including a facsimile transmission of this Agreement, shall be deemed to be an original and shall have the same force and effect as an original. All counterparts together shall constitute but one and the same instrument.

Section 2.10 Applicable Law. The provisions of this Agreement shall be construed in accordance with the laws of the State of Texas, excluding any conflicts of law rule or principle that might refer the construction or interpretation hereof to the laws of another jurisdiction.

Section 2.11 Binding Effect; Assignment. Except for the ability of VCSC to cause one or more of the Administrative Services to be performed by a third party provider or an Affiliate of VCSC, no party shall have the right to assign its rights or obligations under this Agreement without the consent of the other parties.

Section 2.12 Invalidity of Provisions. In the event that one or more of the provisions contained in this Agreement shall be invalid, illegal or unenforceable in any respect under any applicable law, the validity, legality or enforceability of the remaining provisions hereof shall not be affected or impaired thereby.

Section 2.13 Modification; Amendment. This Agreement may be amended or modified from time to time only by a written amendment signed by all parties hereto; provided however, that the Partnership Parties may not, without the prior approval of the Conflicts Committee, agree to any amendment or modification to this Agreement that, in the reasonable discretion of the General Partner, will adversely affect the holders of common units of the Partnership.

Section 2.14 Entire Agreement. This Agreement constitutes the whole and entire agreement between the parties hereto and supersedes any prior agreement, undertaking, declarations, commitments or representations, verbal or oral, in respect of the subject matter hereof.

IN WITNESS WHEREOF, the parties hereto have executed this Agreement with effect as of the date first above written.

DIAMOND SHAMROCK REFINING AND MARKETING COMPANY

By: /s/ Kimberly S. Bowers
Name: Kimberly S. Bowers
Title: Vice President

VALERO CORPORATE SERVICES COMPANY

By: /s/ Michael S. Ciskowski
Name: Michael S. Ciskowski
Title: Executive Vice President

VALERO L.P

By: Riverwalk Logistics, L.P.

By: Valero GP, LLC

By: /s/ Curtis V. Anastasio
Name: Curtis V. Anastasio
Title: President

VALERO LOGISTICS OPERATIONS, L.P.

By: Valero GP, Inc.

By: /s/ Curtis V. Anastasio
Name: Curtis V. Anastasio
Title: President

VALERO GP, LLC

By: /s/ Curtis V. Anastasio
Name: Curtis V. Anastasio
Title: President

RIVERWALK LOGISTICS, L.P.

By: Valero GP, LLC

By: /s/ Curtis V. Anastasio
Name: Curtis V. Anastasio
Title: President

SIGNATURE PAGE TO THIRD AMENDED AND RESTATED SERVICES AGREEMENT

EXHIBIT A

Administrative Services provided to the Partnership Parties:

IS Support
Corporate Tax
Ad Valorem Tax
Human Resources (benefits, compensation, employment, payroll, corporate HR support)
PR/Community Relations
Governmental Affairs
Graphic Services
Risk Control & Analysis
Risk Management
Corporate Records
Corporate Travel/Aviation[(a)]
Office Services[(b)]
Facility Services[(b)]
Corporate Services Department[(b)]
Security Services[(b])
Other Administrative Services as the parties may agree.

In providing the foregoing services, VCSC shall be acting on behalf of and as agent for the Partnership Parties.

Notes:

(a) Aviation Services may be documented under a time-share arrangement, in which case, the Administrative Services Fee will be reduced by $70,250.

(b) Upon the Commencement Date, as that term is defined in that certain Office Lease Agreement between Valero Corporate Services Company and Valero Logistics Operations, L.P., dated as of January 1, 2006 (the “Lease Agreement”), the Administrative Services Fee shall be reduced by $130,000 to account for the assumption of Office Services, Facility Services, Corporate Services and Security that will be provided to the Partnership Parties pursuant to the Lease Agreement.

Memorandum of Understanding
Regarding Office Lease Agreement
Between
Valero Corporate Services Company, as Landlord, and
Valero Logistics Operations, L.P., as Tenant

This Memorandum of Understanding, by and between Valero Corporate Services Company, a Delaware corporation, and Valero Logistics Operations, L.P., a Delaware limited partnership, will serve to document the agreement of such parties on the principal terms of an Office Lease Agreement (the "Lease Agreement") to be executed by the parties. The parties agree to more fully memorialize these agreements in the Lease Agreement no later than March 31, 2006, or such other date as may be mutually agreed to by the parties. Until such Lease Agreement is executed and delivered on behalf of the parties, the terms of this Memorandum of Understanding shall be binding on the parties.

Principal Terms of Lease Agreement:

Landlord:	Valero Corporate Services Company
Tenant:	Valero Logistics Operations, L.P.

Leased Premises: All of a floor (approximately 63,803 square feet, floor to-be-determined) of the to-be-constructed office building (the "Building") totaling approximately 259,455 square feet at Valero corporate headquarters (the "Project"), in San Antonio, Bexar County, Texas, located on that certain parcel of land (the "Land") replatted as Lot 6, Block 2, NCB 14746, recorded in Book 9568, Page 191, Plat Records of Bexar County, Texas.

Effective Date:	January 1, 2006
Initial Term:	25 years from Rent Commencement Date (defined below)
Renewal Option(s):	One (1) option, for a period of 10 years

Rent Commencement Date: The earlier of (i) the Substantial Completion Date (defined below) or (ii) the date of Tenant's beneficial occupancy of the Leased Premises for the conduct of its business therein. For purposes hereof, the "Substantial Completion Date" means the date on which the initial leasehold improvements to the Leased Premises are completed in all material respects in substantial compliance with the final plans and permits and the Leased Premises are ready for occupancy.

Use:	General office use, and related administrative and ancillary purposes
Base Rent:	Initial Term:

For first 5 years: $1,598,000 per year;

For the next 5 years, Base Rent shall be adjusted based on changes in the CPI Index;

Thereafter, at the beginning of each 5 year period for the remainder of the Initial Term, Base Rent shall be adjusted to reflect the actual market rent for comparable office space.

The Base Rent includes Tenant's proportionate share (based on a fraction, the numerator of which is the rentable square footage of the Leased Premises, and the denominator of which is the rentable square footage of the Building and the other buildings at the Project) of (i) Landlord's operating expenses, such as HVAC, janitorial services, and the other Landlord Services (defined below), (ii) the real property ad valorem taxes assessed or imposed on the Project, and (iii) Landlord's insurance costs relating to the Project.

Renewal Period:

At the beginning of the renewal period (if applicable), and again after the expiration of the first 5 years of the renewal period, the Base Rent shall be adjusted to reflect the actual market rent for comparable office space.

Change of Control Provision: In the event of a change of control ("Change of Control") of Valero L.P. or Valero GP Holdings, LLC, Landlord may, in its sole discretion, declare default by Tenant under the lease, for which Landlord will have all remedies available to it under the lease, including the right to evict Tenant with 6 months prior notice (such 6 month notice period shall only apply if the Change of Control is the sole Tenant default).

Remedies upon Tenant Default: Lease shall contain standard Landlord remedies upon Tenant default, including (without limitation) acceleration of rent.

Relocation of Landlord's Headquarters: If Landlord's corporate headquarters are relocated to any other location, Landlord may terminate the Lease on 12 months prior written notice.

Initial Tenant Improvements/Alteration Rights: Landlord shall be responsible, at its sole cost and expense, for initial tenant improvements/finish-out of Leased Premises, based on plans approved by Landlord and Tenant; after the Commencement Date, Tenant may make non-structural changes to the Leased Premises without Landlord's consent (structural changes shall require Landlord's prior written consent, in its sole discretion).

Furnishings & Moving Expenses: Landlord shall provide Tenant with all furnishings being used by Tenant in Landlord's other buildings as of the Rent Commencement Date.

All furnishings required by Tenant after the Rent Commencement Date shall be at Tenant's sole cost and expense. Landlord shall move Tenant into the Leased Premises at its sole cost and expense.

No Representations or Warranties: The Leased Premises shall be leased on an "AS IS", "WITH ALL FAULTS" basis, with no express or implied representations or warranties provided by Landlord; provided that, to the extent that any express warranties from third-party contractors relating to the initial tenant improvements to the Leased Premises are partially assignable to Tenant, Landlord shall partially assign such warranties to Tenant.

Landlord Services/Maintenance Responsibilities; Tenant Maintenance Responsibilities: Landlord shall be responsible for providing (i) maintenance and repair of the roof, exterior walls, foundations and other structural elements of the Building; (ii) the following with respect to the Leased Premises: janitorial services, elevator service, electrical services, HVAC, replacement of lamps and ballasts in ceiling, water and sewer service for the restrooms, and routine plumbing repairs; (iii) grounds and landscaping maintenance; and (iv) parking lot maintenance (collectively, "Landlord Services"). Tenant shall be responsible for providing all other maintenance and repairs to the Leased Premises.

License to Use Certain Amenities: As long as Landlord is providing the Campus Amenities (defined below) to its employees at the Project, then Tenant's employees at the Leased Premises shall have a license to use the Campus Amenities, within the areas at the Project or on Landlord's adjacent campus designated by Landlord in its sole discretion, at no additional cost to Tenant other than any costs charged to Landlord's employees therefor. Notwithstanding the foregoing, Landlord may terminate the license (or any portion thereof, in Landlord's sole discretion) described in this paragraph at any time upon thirty (30) days written notice to Tenant after a Change of Control. For purposes hereof, the term "Campus Amenities" means the following: cafeteria services provided by Aramark Food Services, Inc. (or other entity designated by Landlord in its sole discretion); fitness center, walking/jogging trails, and basketball and tennis courts owned by Landlord at the Project; fitness services provided by MediFit Corporate Services, Inc. (or other entity designated by Landlord in its sole discretion); massage therapy provided by any person or entity designated by Landlord in its sole discretion; and any other similar kinds of services that may be provided by Landlord at the Project to Landlord's employees at the Project in the future, as may be designated by Landlord in its sole discretion.

Tenant's Right to Assign or Sublease: Tenant may not assign any of its interest in the lease or sublet all or any portion of the Leased Premises without Landlord's prior written consent, in Landlord's sole discretion.

Security: Subject to the provisions below, Landlord shall provide security services for the Project, including the parking garage and the Leased Premises.

Indemnity: The lease will contain typical indemnities (contained in standard office leases) from Tenant in favor of Landlord; provided that Tenant shall release, indemnify and hold harmless Landlord from and against any and all claims of Tenant's employees arising from the security, health, and/or fitness services (each of which is described above) at the Project or the exercise of any of the rights under the license described above by Tenant's employees, including, without limitation, any such claim caused by or resulting from Landlord's negligence. The lease will include the necessary provisions to comply with the express negligence standards of the laws of the State of Texas.

Insurance: The lease will describe the insurance coverage (as typically required by Landlord) that Tenant shall provide at its sole cost and expense, with Landlord named as an additional insured.

Taxes: Tenant shall be responsible for payment of all taxes and assessments levied or assessed upon Tenant's fixtures, furniture and personal property located in or about the Leased Premises.

Parking: Tenant shall be entitled to a pro-rata share of the parking spaces located in the parking garage to be constructed adjacent to the Building, including a pro-rata share of the reserved spaces, based on its proportionate share (made up of a fraction, the numerator of which is the rentable square footage of the Leased Premises in the Building, and the denominator of which is the rentable square footage in the Building), all at no additional cost.

Brokerage Commissions: None. The lease shall contain a mutual indemnity for any claim for brokerage commissions in connection with the lease arising by, through or under the indemnifying party.

The parties agree that this Memorandum of Understanding shall be binding upon their respective successors and assigns, and that either party may assign its rights and obligations hereunder to one or more affiliates without the other party's prior written consent. This Memorandum of Understanding may be amended only by an instrument in writing signed by both parties. This Memorandum of Understanding shall be superseded by the Lease Agreement upon the complete execution of the Lease Agreement. THIS MEMORANDUM OF UNDERSTANDING SHALL BE GOVERNED BY AND CONSTRUED IN ACCORDANCE WITH THE LAWS OF THE STATE OF TEXAS. THIS MEMORANDUM OF UNDERSTANDING WAS PREPARED BY BOTH PARTIES HERETO AND NOT BY ONE PARTY TO THE EXCLUSION OF THE OTHER PARTY.

[signatures contained on next page]

The parties, by the signature of the duly authorized officers below, agree to terms set forth above, effective as of January 1, 2006.

“Landlord”
VALERO CORPORATE SERVICES COMPANY

By: /s/ Mike Ciskowski
Mike Ciskowski, Executive Vice President

“Tenant”
VALERO LOGISTICS OPERATIONS, L.P.

By: Valero GP, Inc., its General Partner

By: /s/ Curtis V. Anastasio
CurtisV. Anastasio, President

Exhibit 12.01

VALERO L.P.
STATEMENT OF COMPUTATION OF RATIO OF EARNINGS TO FIXED CHARGES
(Thousands of Dollars, Except Ratio)

	Quarter Ended March 31, 2006	Year Ended December 31, 2005	2004	2003	2002	2001
Earnings:						
Income from continuing operations before provision for income taxes and income from equity investees	$40,502	$110,069	$77,074	$67,177	$52,350	$42,694
Add:						
Fixed charges	17,914	46,211	21,625	16,443	5,492	4,203
Amortization of capitalized interest	26	80	60	55	48	39
Distributions from joint ventures	1,524	4,657	1,373	2,803	3,590	2,874
Less: Interest capitalized	(468)	(1,008)	(192)	(123)	(255)	(298)
Total earnings	$59,498	$160,009	$99,940	$86,355	$61,225	$49,512
Fixed charges:						
Interest expense (1)	$15,994	$ 41,616	$20,630	$15,291	$ 4,968	$ 3,721
Amortization of debt issuance costs	179	622	407	740	160	90
Interest capitalized	468	1,008	192	123	255	298
Rental expense interest factor (2)	1,273	2,965	396	289	109	94
Total fixed charges	$17,914	$ 46,211	$21,625	$16,443	$ 5,492	$ 4,203
Ratio of earnings to fixed charges	3.3x	3.5x	4.6x	5.3x	11.1x	11.8x

(1) The "interest and other expenses, net" reported in Valero L.P.'s consolidated statements of income for the three months ended March 31, 2006 and the year ended December 31, 2005 includes investment income of $477,000 and $850,000, respectively and includes other income (expense) of $231,000 and ($2,237,000), respectively.

(2) The interest portion of rental expense represents one-third of rents, which is deemed representative of the interest portion of rental expense.

Exhibit 31.01

CERTIFICATION PURSUANT TO SECTION 302
OF THE SARBANES-OXLEY ACT OF 2002

I, Curtis V. Anastasio, the principal executive officer of Valero GP, LLC, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Valero L.P. (the “registrant”);

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant’s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and

5. The registrant’s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

Date: May 9, 2006

/s/ Curtis V. Anastasio
Curtis V. Anastasio
President and Chief Executive Officer

**CERTIFICATION PURSUANT TO SECTION 302
OF THE SARBANES-OXLEY ACT OF 2002**

I, Steven A. Blank, the principal financial officer of Valero GP, LLC, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Valero L.P. (the "registrant");

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 9, 2006

/s/ Steven A. Blank
Steven A. Blank
Senior Vice President and Chief Financial Officer

Exhibit 32.01

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of Valero L.P. (the Partnership) on Form 10-Q for the quarter ended March 31, 2006, as filed with the Securities and Exchange Commission on the date hereof (the Report), I, Curtis V. Anastasio, President and Chief Executive Officer of Valero GP, LLC, hereby certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Partnership.

/s/ Curtis V. Anastasio
Curtis V. Anastasio
President and Chief Executive Officer
May 9, 2006

A signed original of the written statement required by Section 906 has been provided to Valero L.P. and will be retained by Valero L.P. and furnished to the Securities and Exchange Commission or its staff upon request.

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of Valero L.P. (the Partnership) on Form 10-Q for the quarter ended March 31, 2006, as filed with the Securities and Exchange Commission on the date hereof (the Report), I, Steven A. Blank, Senior Vice President and Chief Financial Officer of Valero GP, LLC, hereby certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Partnership.

/s/ Steven A. Blank

Steven A. Blank
Senior Vice President and Chief Financial Officer
May 9, 2006

A signed original of the written statement required by Section 906 has been provided to Valero L.P. and will be retained by Valero L.P. and furnished to the Securities and Exchange Commission or its staff upon request.