STAR GAS PARTNERS LP
Form 10-Q
February 03, 2016
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended December 31, 2015

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: 001-14129

STAR GAS PARTNERS, L.P.

(Exact name of registrants as specified in its charters)

Delaware	**06-1437793**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
9 West Broad Street Stamford, Connecticut	**06902**
(Address of principal executive office)	

(203) 328-7310

(Registrant s telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨

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

Large accelerated filer ¨	Accelerated filer x
Non-accelerated filer ¨	Smaller reporting company ¨

Indicate by check mark whether the registrants are shell companies (as defined in Rule 12b-2 of the Act). Yes ¨ No x

At January 31, 2016, the registrant had 57,279,052 Common Units outstanding.

STAR GAS PARTNERS, L.P. AND SUBSIDIARIES

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Part I. FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statements

STAR GAS PARTNERS, L.P. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands)	December 31, 2015 (unaudited)	September 30, 2015
ASSETS		
Current assets		
Cash and cash equivalents	$ 86,890	$ 100,508
Receivables, net of allowance of $6,287 and $6,713, respectively	112,141	89,230
Inventories	64,881	55,671
Fair asset value of derivative instruments	405	935
Weather hedge contract receivable	12,500	
Current deferred tax assets, net	37,460	37,832
Prepaid expenses and other current assets	24,290	25,135
Total current assets	338,567	309,311
Property and equipment, net	69,687	68,123
Goodwill	212,676	211,045
Intangibles, net	107,332	107,317
Deferred charges and other assets, net	12,361	11,236
Total assets	$ 740,623	$ 707,032
LIABILITIES AND PARTNERS CAPITAL		
Current liabilities		
Accounts payable	$ 21,624	$ 25,322
Fair liability value of derivative instruments	21,523	12,819
Current maturities of long-term debt	10,000	10,000
Accrued expenses and other current liabilities	107,486	107,745
Unearned service contract revenue	55,291	44,419
Customer credit balances	88,798	78,207
Total current liabilities	304,722	278,512
Long-term debt	90,000	90,000
Long-term deferred tax liabilities, net	22,028	21,524

Other long-term liabilities	27,123	27,110
Partners capital		
Common unitholders	319,238	312,713
General partner	(325)	(283)
Accumulated other comprehensive loss, net of taxes	(22,163)	(22,544)
Total partners capital	296,750	289,886
Total liabilities and partners capital	$ 740,623	$ 707,032

See accompanying notes to condensed consolidated financial statements.

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STAR GAS PARTNERS, L.P. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per unit data - unaudited)	Three Months Ended December 31, 2015	Three Months Ended December 31, 2014
Sales:		
Product	$ 252,950	$ 435,012
Installations and services	66,105	64,205
Total sales	319,055	499,217
Cost and expenses:		
Cost of product	150,102	309,249
Cost of installations and services	62,912	60,683
(Increase) decrease in the fair value of derivative instruments	5,536	8,290
Delivery and branch expenses	64,194	78,834
Depreciation and amortization expenses	6,766	6,158
General and administrative expenses	6,420	6,056
Finance charge income	(521)	(826)
Operating income	23,646	30,773
Interest expense, net	(1,859)	(3,460)
Amortization of debt issuance costs	(312)	(400)
Income before income taxes	21,475	26,913
Income tax expense	9,417	11,359
Net income	$ 12,058	$ 15,554
General Partner s interest in net income	68	88
Limited Partners interest in net income	$ 11,990	$ 15,466
Basic and diluted income per Limited Partner Unit (1):	$ 0.19	$ 0.24
Weighted average number of Limited Partner units outstanding:		
Basic and Diluted	57,281	57,294

(1) See Note 13 Earnings Per Limited Partner Unit.

See accompanying notes to condensed consolidated financial statements.

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STAR GAS PARTNERS, L.P. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(in thousands - unaudited)	**Three Months Ended December 31, 2015**	**2014**
Net income	$ 12,058	$ 15,554
Other comprehensive income:		
Unrealized gain on pension plan obligation (1)	648	556
Tax effect of unrealized gain on pension plan	(267)	(230)
Total other comprehensive income	381	326
Total comprehensive income	$ 12,439	$ 15,880

(1) This item is included in the computation of net periodic pension cost.

See accompanying notes to condensed consolidated financial statements.

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STAR GAS PARTNERS, L.P. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENT OF PARTNERS CAPITAL

(in thousands - unaudited)	Number of Units Common	Number of Units General Partner	Common	General Partner	Accum. Other Comprehensive Income (Loss)	Total Partners Capital
Balance as of September 30, 2015	57,282	326	$ 312,713	$ (283)	$ (22,544)	$ 289,886
Net income			11,990	68		12,058
Unrealized gain on pension plan obligation					648	648
Tax effect of unrealized gain on pension plan					(267)	(267)
Distributions			(5,442)	(110)		(5,552)
Retirement of units (1)	(3)		(23)			(23)
Balance as of December 31, 2015 (unaudited)	57,279	326	$ 319,238	$ (325)	$ (22,163)	$ 296,750

(1) See Note 3 - Common Unit Repurchase and Retirement.

See accompanying notes to condensed consolidated financial statements.

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STAR GAS PARTNERS, L.P. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands - unaudited)	**Three Months Ended December 31, 2015**	**2014**
Cash flows provided by (used in) operating activities:		
Net income	$ 12,058	$ 15,554
Adjustment to reconcile net income to net cash provided by (used in) operating activities:		
(Increase) decrease in fair value of derivative instruments	5,536	8,290
Depreciation and amortization	7,078	6,558
Provision for losses on accounts receivable	(636)	236
Change in deferred taxes	609	230
Change in weather hedge contract receivable	(12,500)	
Changes in operating assets and liabilities:		
Increase in receivables	(22,263)	(58,241)
Increase in inventories	(9,064)	(8,633)
(Increase) decrease in other assets	1,091	(5,565)
Increase (decrease) in accounts payable	(3,020)	20,261
Increase (decrease) in customer credit balances	10,427	(5,862)
Increase in other current and long-term liabilities	13,883	13,752
Net cash provided by (used in) operating activities	3,199	(13,420)
Cash flows provided by (used in) investing activities:		
Capital expenditures	(3,206)	(1,772)
Proceeds from sales of fixed assets	23	88
Acquisitions	(7,615)	
Net cash used in investing activities	(10,798)	(1,684)
Cash flows provided by (used in) financing activities:		
Distributions	(5,552)	(5,098)
Unit repurchases	(23)	(691)
Customer retainage payments	(235)	
Payments of debt issue costs	(209)	
Net cash used in financing activities	(6,019)	(5,789)
Net decrease in cash and cash equivalents	(13,618)	(20,893)
Cash and cash equivalents at beginning of period	100,508	48,999

Cash and cash equivalents at end of period	$ 86,890	$ 28,106

See accompanying notes to condensed consolidated financial statements.

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STAR GAS PARTNERS, L.P. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1) Partnership Organization

Star Gas Partners, L.P. (Star Gas Partners, the Partnership, we, us, or our) is a full service provider specializing i sale of home heating products and services to residential and commercial customers. The Partnership also services and sells heating and air conditioning equipment to its home heating oil and propane customers and to a lesser extent, provides these offerings to customers outside of our home heating oil and propane customer base. In certain of our marketing areas, we provide home security and plumbing services primarily to our home heating oil and propane customer base. We also sell diesel fuel, gasoline and home heating oil on a delivery only basis. These products and services are offered through our home heating oil and propane locations. The Partnership has one reportable segment for accounting purposes. We are the nation s largest retail distributor of home heating oil based upon sales volume. Including our propane locations, we serve customers in the more northern and eastern states within the Northeast, Central and Southeast U.S. regions.

The Partnership is organized as follows:

The Partnership is a master limited partnership, which as of December 31, 2015, had outstanding 57.3 million Common Units (NYSE: SGU), representing 99.43% limited partner interest in Star Gas Partners, and 0.3 million general partner units, representing 0.57% general partner interest in Star Gas Partners. The general partner of the Partnership is Kestrel Heat, LLC, a Delaware limited liability company (Kestrel Heat or the general partner). The Board of Directors of Kestrel Heat (the Board) is appointed by its sole member, Kestrel Energy Partners, LLC, a Delaware limited liability company (Kestrel).

The Partnership owns 100% of Star Acquisitions, Inc., a Minnesota corporation (SA), that owns 100% of Petro Holdings, Inc., a Minnesota corporation (Petro). SA and its subsidiaries are subject to Federal and state corporate income taxes. The Partnership s operations are conducted through Petro and its subsidiaries. Petro is primarily a Northeast, Central and Southeast region retail distributor of home heating oil and propane that as of December 31, 2015, served approximately 458,000 full-service residential and commercial home heating oil and propane customers. Petro also sold diesel fuel, gasoline and home heating oil to approximately 78,000 customers on a delivery only basis. In addition, Petro installed, maintained, and repaired heating and air conditioning equipment for its customers and provided ancillary home services, including home security and plumbing, to approximately 25,000 customers.

Petroleum Heat and Power Co., Inc., a Minnesota corporation (PH&P) is a 100% owned subsidiary of the Partnership. PH&P is the borrower and the Partnership is the guarantor of the third amended and restated credit agreement s $100 million five-year senior secured term loan and the $300 million ($450 million during the heating season of December through April of each year) revolving credit facility, both due July 30, 2020. (See Note 9 Long-Term Debt and Bank Facility Borrowings)

2) Summary of Significant Accounting Policies

Basis of Presentation

The Consolidated Financial Statements include the accounts of Star Gas Partners and its subsidiaries. All material inter-company items and transactions have been eliminated in consolidation.

The financial information included herein is unaudited; however, such information reflects all adjustments (consisting solely of normal recurring adjustments), which are, in the opinion of management, necessary for the fair statement of financial condition and results for the interim periods. Due to the seasonal nature of the Partnership s business, the results of operations and cash flows for the three month period ended December 31, 2015, and December 31, 2014, are not necessarily indicative of the results to be expected for the full year.

These interim financial statements of the Partnership have been prepared in accordance with U.S. Generally Accepted Accounting Principles (GAAP) for interim financial information and Rule 10-01 of Regulation S-X of the U.S. Securities and Exchange Commission and should be read in conjunction with the financial statements included in the Partnership s Annual Report on Form 10-K for the year ended September 30, 2015.

Comprehensive Income (Loss)

Comprehensive income (loss) is comprised of net income (loss) and other comprehensive income (loss). Other comprehensive income (loss) consists of the unrealized gain (loss) amortization on the Partnership s pension plan obligation for its two frozen defined benefit pension plans and the corresponding tax effect.

Weather Hedge Contract

To partially mitigate the adverse effect of warm weather on cash flows, the Partnership has used weather hedge contracts for a number of years. Weather hedge contracts are recorded in accordance with the intrinsic value method defined by the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 815-45-15 Derivatives and Hedging, Weather Derivatives (EITF 99-2). The premium paid is included in the caption prepaid expenses and other current assets in the accompanying balance sheets and amortized over the life of the contract, with the intrinsic value method applied at each interim period.

For fiscal years 2016 and 2017 the Partnership has a weather hedge contract with Swiss Re under which the Partnership is entitled to receive a payment of $35,000 per heating degree-day shortfall, when the accumulated number of heating degree-days in the entire hedge period is less than approximately 92.5% of the ten year average, the Payment Threshold as defined in the contract. The hedge covers the five month period from November 1, through March 31, taken as a whole, for each respective fiscal year. The ultimate amount due to the Partnership (if any) is based on the entire five month accumulated calculation for the hedge period and has a maximum payout of $12.5 million for each respective fiscal year. In accordance with ASC 815-45-15, as of December 31, 2015, the Partnership recorded a credit of $12.5 million under this contract that reduced delivery and branch expenses. The final credit (if any) for fiscal 2016 may be lower than this amount depending on the actual heating degree-days recorded in the period January 1, 2016 through March 31, 2016. If the heating degree-days in this period approximate normal, the credit will be reduced to approximately $5.2 million. If temperatures in this period are colder than expected, then the additional heating degree-days could reduce the credit further, possibly even to zero. Temperatures recorded for January 2016, were slightly warmer than expected.

New England Teamsters and Trucking Industry Pension Fund (the NETTI Fund) Liability

As of December 31, 2015 we had $0.1 million and $17.6 million balances included in the captions accrued expenses and other current liabilities and other long-term liabilities, respectively, on our condensed consolidated balance sheet representing the remaining balance of the NETTI withdrawal liability. Based on the borrowing rates currently available to the Partnership for long-term financing of a similar maturity, the fair value of the NETTI withdrawal liability as of December 31, 2015 was $16.0 million. We utilized Level 2 inputs in the fair value hierarchy of valuation techniques to determine the fair value of this liability.

Recent Accounting Pronouncements

In May 2014, the FASB issued Accounting Standards Update (ASU) No. 2014-09, Revenue from Contracts with Customers, which requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. This ASU will replace most existing revenue recognition guidance in GAAP when it becomes effective. This new guidance is effective for our annual reporting period beginning in the first quarter of fiscal 2019, with early adoption permitted beginning in the first quarter of fiscal 2018. The standard permits the use of either the retrospective or cumulative effect transition method. The Partnership is evaluating the effect that ASU 2014-09 will have on its consolidated financial statements and related disclosures. The Partnership has not yet selected a transition method nor has it determined the timing of adoption.

In April 2015, the FASB issued ASU No. 2015-03, Interest - Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs. The update requires debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of the related debt liability instead of being presented as an asset. The update requires retrospective application and represents a change in accounting principle. The update is effective for our annual reporting period beginning in the first quarter of fiscal 2017, with early adoption permitted. The Partnership expects the impact of ASU No. 2015-03 will be limited to the presentation of debt issuance cost on its balance sheet.

In July 2015, the FASB issued ASU No. 2015-11, Simplifying the Measurement of Inventory. The update changes the measurement principle for inventory from the lower of cost or market to the lower of cost and net realizable value. This new guidance is effective for our annual reporting period beginning in the first quarter of fiscal 2018, with early adoption permitted. The Partnership does not expect ASU No. 2015-11 to have a material impact on its consolidated financial statements and related disclosures.

In September 2015, the FASB issued ASU No. 2015-16, Simplifying the Accounting for Measurement-Period Adjustments, which requires an acquiring entity to recognize adjustments to provisional amounts that are identified during the measurement period in the reporting period in which the adjustment amounts are determined. The acquiring entity is required to record, in the same period s financial statements, the effect on earnings of changes in depreciation, amortization, or other income effects, if any, as a result of the change to the provisional amounts, calculated as if the accounting had been completed at the acquisition date. In addition, the acquiring entity is to present separately on the face of its income statement or disclose in the notes the portion of the amount recorded in current-period earnings by line item that would have been recorded in previous reporting periods as if the adjustment to the provisional amounts had been recognized as of the acquisition date. This new guidance is effective for our annual reporting period beginning in the first quarter of fiscal 2017. The Partnership does not expect ASU No. 2015-16 to have a material impact on its consolidated financial statements and related disclosures.

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In November 2015, FASB issued ASU 2015-17, Income Taxes - Balance Sheet Classification of Deferred Taxes, which eliminates the requirement for companies to present deferred tax assets and liabilities as current and non-current in a classified balance sheet. Instead, companies will be required to classify all deferred tax assets and liabilities as non-current. This new guidance is effective for our annual reporting period beginning in the first quarter of fiscal 2018, with early adoption permitted. The standard permits the use of either the prospective or retrospective transition method. The Partnership is evaluating the effect that ASU No. 2015-17 will have on its consolidated financial statements and related disclosures. The Partnership has not yet selected a transition method nor has it determined the timing of adoption.

3) Common Unit Repurchase and Retirement

In July 2012, the Board authorized the repurchase of up to 3.0 million of the Partnership s Common Units (Plan III). In July 2013, the Board authorized the repurchase of an additional 1.9 million Common Units under Plan III. The authorized Common Unit repurchases may be made from time to time in the open market, in privately negotiated transactions or in such other manner deemed appropriate by management. There is no guarantee of the exact number of units that will be purchased under the program and the Partnership may discontinue purchases at any time. The program does not have a time limit. The Board may also approve additional purchases of units from time to time in private transactions. The Partnership s repurchase activities take into account SEC safe harbor rules and guidance for issuer repurchases. All of the Common Units purchased in the repurchase program will be retired.

Under the Partnership s third amended and restated credit agreement dated July 30, 2015, in order to repurchase Common Units we must maintain Availability (as defined in the amended and restated credit agreements) of $45 million, 15.0% of the facility size of $300 million (assuming the non-seasonal aggregate commitment is in effect) on a historical pro forma and forward-looking basis, and a fixed charge coverage ratio of not less than 1.15 measured as of the date of repurchase. The Partnership was in compliance with this covenant for all unit repurchases made during the three months ended December 31, 2015.

The following table shows repurchases under Plan III.

(in thousands, except per unit amounts) **Period**	**Total Number of Units Purchased (a)**	**Average Price Paid per Unit (b)**	**Maximum Number of Units that May Yet Be Purchased**
Plan III - Number of units authorized			**4,894**
Private transaction - Number of units authorized			**1,150**
			6,044
Plan III - Fiscal years 2012 to 2015 total (c)	3,742	$ 4.72	2,302
Plan III - October 2015		$	2,302
Plan III - November 2015		$	2,302
Plan III - December 2015	3	$ 7.02	2,299

Plan III - First quarter fiscal year 2016 total	3	$	7.02	2,299

(a) Units were repurchased as part of a publicly announced program, except as noted in a private transaction.
(b) Amounts include repurchase costs.
(c) Includes 1.4 million common units acquired in a private transaction.

4) Derivatives and Hedging Disclosures and Fair Value Measurements

FASB ASC 815-10-05 Derivatives and Hedging, established accounting and reporting standards requiring that derivative instruments be recorded at fair value and included in the consolidated balance sheet as assets or liabilities, along with qualitative disclosures regarding the derivative activity. The Partnership uses derivative instruments such as futures, options and swap agreements in order to mitigate exposure to market risk associated with the purchase of home heating oil for price-protected customers, physical inventory on hand, inventory in transit, priced purchase commitments and internal fuel usage. The Partnership has elected not to designate its derivative instruments as hedging derivatives, but rather as economic hedges whose change in fair value is recognized in its statement of operations in the line item (increase) decrease in the fair value of derivative instruments. Depending on the risk being economically hedged, realized gains and losses are recorded in cost of product, cost of installations and services, or delivery and branch expenses.

As of December 31, 2015, to hedge a substantial majority of the purchase price associated with heating oil gallons anticipated to be sold to its price-protected customers, the Partnership held the following derivative instruments that settle in future months to match anticipated sales: 10.1 million gallons of swap contracts, 8.2 million gallons of call options, 6.0 million gallons of put options, and 98.9 million net gallons of synthetic call options. To hedge the inter-month differentials for its price-protected customers, its physical inventory on hand and inventory in transit, the Partnership, as of December 31, 2015, had 1.4 million gallons of long swap contracts, 24.6 million gallons of long future contracts, and 57.1 million gallons of short future contracts that settle in future months. In addition to the previously described hedging instruments, to lock-in the differential between high sulfur home heating oil and ultra low sulfur diesel, the Partnership as of December 31, 2015, had 8.4 million gallons of spread contracts (simultaneous long and short positions). To hedge its internal fuel usage and other related activities for fiscal 2016, the Partnership, as of December 31, 2015, had 4.4 million gallons of swap contracts that settle in future months.

As of December 31, 2014, to hedge a substantial majority of the purchase price associated with heating oil gallons anticipated to be sold to its price-protected customers, the Partnership held the following derivative instruments that settle in future months to match anticipated sales: 12.4 million gallons of swap contracts, 5.6 million gallons of call options, 7.7 million gallons of put options, and 94.1 million net gallons of synthetic call options. To hedge the inter-month differentials for its price-protected customers, its physical inventory on hand and inventory in transit, the Partnership, as of December 31, 2014, had 29.6 million gallons of long future contracts, and 55.1 million gallons of short future contracts that settle in future months. To hedge its internal fuel usage for fiscal 2015, the Partnership as of December 31, 2014, had 2.9 million gallons of swap contracts that settle in future months.

The Partnership s derivative instruments are with the following counterparties: Bank of America, N.A., Bank of Montreal, Cargill, Inc., Citibank, N.A., JPMorgan Chase Bank, N.A., Key Bank, N.A., Munich Re Trading LLC, Regions Financial Corporation, Societe Generale, and Wells Fargo Bank, N.A. The Partnership assesses counterparty credit risk and considers it to be low. We maintain master netting arrangements that allow for the non-conditional offsetting of amounts receivable and payable with counterparties to help manage our risks and record derivative positions on a net basis. The Partnership generally does not receive cash collateral from its counterparties and does not restrict the use of cash collateral it maintains at counterparties. At December 31, 2015, the aggregate cash posted as collateral in the normal course of business at counterparties was $2.6 million ($2.3 million recorded in prepaid expenses and other current assets and $0.3 million recorded in fair liability value of derivative instruments). Positions with counterparties who are also parties to our credit agreement are collateralized under that facility. As of December 31, 2015, $24.8 million of hedge positions and payable amounts were secured under the credit facility.

FASB ASC 820-10 Fair Value Measurements and Disclosures, established a three-tier fair value hierarchy, which classified the inputs used in measuring fair value. These tiers include: Level 1, defined as observable inputs such as quoted prices for identical instruments in active markets; Level 2, defined as inputs other than quoted prices in active markets that are either directly or indirectly observable; and Level 3, defined as unobservable inputs in which little or no market data exists, therefore requiring an entity to develop its own assumptions. The Partnership s Level 1 derivative assets and liabilities represent the fair value of commodity contracts used in its hedging activities that are identical and traded in active markets. The Partnership s Level 2 derivative assets and liabilities represent the fair value of commodity contracts used in its hedging activities that are valued using either directly or indirectly observable inputs, whose nature, risk and class are similar. No significant transfers of assets or liabilities have been made into and out of the Level 1 or Level 2 tiers. All derivative instruments were non-trading positions and were either a Level 1 or Level 2 instrument. The Partnership had no Level 3 derivative instruments. The fair market value of our Level 1 and Level 2 derivative assets and liabilities are calculated by our counter-parties and are independently validated by the Partnership. The Partnership s calculations are, for Level 1 derivative assets and liabilities, based on the published New York Mercantile Exchange (NYMEX) market prices for the commodity contracts open at the end of the period. For Level 2 derivative assets and liabilities the calculations performed by the Partnership are based on a combination of the NYMEX published market prices and other inputs, including such factors as present value, volatility and duration.

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The Partnership had no assets or liabilities that are measured at fair value on a nonrecurring basis subsequent to their initial recognition. The Partnership s financial assets and liabilities measured at fair value on a recurring basis are listed on the following table.

(In thousands)		Fair Value Measurements at Reporting Date Using:		
Derivatives Not Designated as Hedging Instruments Under FASB ASC 815-10	**Balance Sheet Location**	**Total**	**Quoted Prices in Active Markets for Identical Assets Level 1**	**Significant Other Observable Inputs Level 2**
	Asset Derivatives at December 31, 2015			
Commodity contracts	Fair asset and fair liability value of derivative instruments	$ 51,220	$ 6,670	$ 44,550
Commodity contracts	Long-term derivative assets included in the other long-term liabilities balance	9,216	4,586	4,630
Commodity contract assets at December 31, 2015		**$ 60,436**	**$ 11,256**	**$ 49,180**
	Liability Derivatives at December 31, 2015			
Commodity contracts	Fair liability and fair asset value of derivative instruments	$ (72,658)	$ (6,265)	$ (66,393)
Commodity contracts	Cash collateral	320	320	
Commodity contracts	Long-term derivative liabilities included in the other long-term liabilities balance	(9,041)	(3,489)	(5,552)
Commodity contract liabilities at December 31, 2015		**$ (81,379)**	**$ (9,434)**	**$ (71,945)**
	Asset Derivatives at September 30, 2015			
Commodity contracts	Fair asset and fair liability value of derivative instruments	$ 26,628	$ 930	$ 25,698
Commodity contracts	Long-term derivative assets included in the other long-term liabilities balance	4,975	2,017	2,958

Commodity contract assets at September 30, 2015		**$ 31,603**	**$ 2,947**	**$ 28,656**

Liability Derivatives at September 30, 2015

Commodity contracts	Fair liability and fair asset value of derivative instruments	$ (41,270)	$	$ (41,270)
Commodity contracts	Cash collateral	2,758	2,758	
Commodity contracts	Long-term derivative liabilities included in the other long-term liabilities balance	(5,977)	(2,038)	(3,939)
Commodity contract liabilities at September 30, 2015		**$ (44,489)**	**$ 720**	**$ (45,209)**

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The Partnership s derivative assets (liabilities) offset by counterparty and subject to an enforceable master netting arrangement are listed on the following table.

(In thousands) Offsetting of Financial Assets (Liabilities) and Derivative Assets (Liabilities)	Gross Assets Recognized	Gross Liabilities Offset in the Statement of Financial Position	Net Assets (Liabilities) Presented in the Statement of Financial Position	Gross Amounts Not Offset in the Statement of Financial Position: Financial Instruments	Cash Collateral Received	Net Amount
Fair asset value of derivative instruments	$ 6,670	$ (6,265)	$ 405	$	$	$ 405
Long-term derivative assets included in deferred charges and other assets, net	$ 5,162	$ (3,918)	$ 1,244	$	$	$ 1,244
Fair liability value of derivative instruments	44,550	(66,073)	(21,523)			(21,523)
Long-term derivative liabilities included in other long-term liabilities, net	4,054	(5,123)	(1,069)			(1,069)
Total at December 31, 2015	$ 60,436	$ (81,379)	$ (20,943)	$	$	$ (20,943)
Fair asset value of derivative instruments	$ 935	$	$ 935	$	$	$ 935
Fair liability value of derivative instruments	25,693	(38,512)	(12,819)			(12,819)
Long-term derivative liabilities included in other long-term liabilities, net	4,975	(5,977)	(1,002)			(1,002)
Total at September 30, 2015	$ 31,603	$ (44,489)	$ (12,886)	$	$	$ (12,886)

(In thousands)

The Effect of Derivative Instruments on the Statement of Operations

Derivatives Not Designated as Hedging Instruments Under FASB ASC 815-10	Location of (Gain) or Loss Recognized in Income on Derivative	Amount of (Gain) or Loss Recognized: Three Months Ended December 31, 2015	Three Months Ended December 31, 2014
Commodity contracts	Cost of product (a)	$ (3,434)	$ (6,805)
Commodity contracts	Cost of installations and service (a)	$ 226	$ 486
Commodity contracts	Delivery and branch expenses (a)	$ 315	$ 474
Commodity contracts		$ 5,536	$ 8,290

(Increase) / decrease in the fair value of derivative instruments

(a) Represents realized closed positions and includes the cost of options as they expire.

5) Inventories

The Partnership s product inventories are stated at the lower of cost or market computed on the weighted average cost method. All other inventories, representing parts and equipment are stated at the lower of cost or market using the FIFO method. The components of inventory were as follows (in thousands):

	December 31, 2015	September 30, 2015
Product	$ 44,656	$ 35,599
Parts and equipment	20,225	20,072
Total inventory	$ 64,881	$ 55,671

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6) Property and Equipment

Property and equipment are stated at cost. Depreciation is computed over the estimated useful lives of the depreciable assets using the straight-line method (in thousands):

	December 31, 2015	September 30, 2015
Property and equipment	$ 178,356	$ 179,631
Less: accumulated depreciation	108,669	111,508
Property and equipment, net	$ 69,687	$ 68,123

7) Business Combination

During fiscal 2016, the Partnership acquired a motor fuel dealer and a propane dealer for an aggregate purchase price of approximately $7.6 million. The gross purchase price was allocated $3.8 million to intangible assets, $1.6 million to goodwill, $2.1 million to fixed assets and $0.1 million to working capital. The acquired company s operating results are included in the Partnership s consolidated financial statements starting on its acquisition date, and are not material to the Partnership s financial condition, results of operations, or cash flows.

8) Goodwill and Intangibles, net

Goodwill

A summary of changes in the Partnership s goodwill is as follows (in thousands):

Balance as of September 30, 2015	$ 211,045
Fiscal year 2016 business combination	1,631
Balance as of December 31, 2015	$ 212,676

Intangibles, net

The gross carrying amount and accumulated amortization of intangible assets subject to amortization are as follows (in thousands):

	December 31, 2015			September 30, 2015		
	Gross Carrying Amount	Accum. Amortization	Net	Gross Carrying Amount	Accum. Amortization	Net
Customer lists	$ 325,594	$ 239,868	$ 85,726	$ 322,027	$ 236,438	$ 85,589
Trade names and other intangibles	26,998	5,392	21,606	26,774	5,046	21,728

Total	$ 352,592	$ 245,260	$ 107,332	$ 348,801	$ 241,484	$ 107,317

Amortization expense for intangible assets was $3.8 million for the three months ended December 31, 2015, compared to $3.3 million for the three months ended December 31, 2014.

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9) Long-Term Debt and Bank Facility Borrowings

The Partnership s debt is as follows (in thousands):	December 31, 2015		September 30, 2015	
	Carrying Amount	Fair Value (a)	Carrying Amount	Fair Value (a)
Revolving Credit Facility Borrowings	$	$	$	$
Senior Secured Term Loan	100,000	100,000	100,000	100,000
Total debt	$ 100,000	$ 100,000	$ 100,000	$ 100,000
Total short-term portion of debt	$ 10,000	$ 10,000	$ 10,000	$ 10,000
Total long-term portion of debt	$ 90,000	$ 90,000	$ 90,000	$ 90,000

(a) The face amount of the Partnership s variable rate long-term debt approximates fair value.

On July 30, 2015, the Partnership entered into a third amended and restated asset based credit agreement with a bank syndicate comprised of thirteen participants, which enables the Partnership to borrow up to $300 million ($450 million during the heating season of December through April of each year) on a revolving credit facility for working capital purposes (subject to certain borrowing base limitations and coverage ratios), provides for a $100 million five-year senior secured term loan (the $100 million Term Loan), allows for the issuance of up to $100 million in letters of credit, and has a maturity date of July 30, 2020.

The Partnership can increase the revolving credit facility size by $100 million without the consent of the bank group. However, the bank group is not obligated to fund the $100 million increase. If the bank group elects not to fund the increase, the Partnership can add additional lenders to the group, with the consent of the Agent, which shall not be unreasonably withheld. Obligations under the third amended and restated credit facility are guaranteed by the Partnership and its subsidiaries and are secured by liens on substantially all of the Partnership s assets including accounts receivable, inventory, general intangibles, real property, fixtures and equipment.

All amounts outstanding under the third amended and restated revolving credit facility become due and payable on the facility termination date of July 30, 2020. The $100 million Term Loan is repayable in quarterly payments of $2.5 million, plus an annual payment equal to 25% of the annual Excess Cash Flow as defined in the agreement (an amount not to exceed $15 million annually), less certain voluntary prepayments made during the year, with final payment at maturity.

The interest rate on the third amended and restated revolving credit facility and the term loan is based on a margin over LIBOR or a base rate. At December 31, 2015, the effective interest rate on the term loan was approximately 3.57%.

The Commitment Fee on the unused portion of the revolving credit facility is 0.30% from December through April, and 0.20% from May through November.

The third amended and restated credit agreement requires the Partnership to meet certain financial covenants, including a fixed charge coverage ratio (as defined in the credit agreement) of not less than 1.1 as long as the $100 million Term Loan is outstanding or revolving credit facility availability is less than 12.5% of the facility size. In addition, as long as the $100 million Term Loan is outstanding, a senior secured leverage ratio at any time cannot be more than 3.0 as calculated during the quarters ending June or September, and at any time no more than 4.5 as calculated during the quarters ending December or March.

Certain restrictions are also imposed by the agreement, including restrictions on the Partnership s ability to incur additional indebtedness, to pay distributions to unitholders, to pay certain inter-company dividends or distributions, make investments, grant liens, sell assets, make acquisitions and engage in certain other activities.

At December 31, 2015, $100.0 million of the term loan was outstanding, no amount was outstanding under the revolving credit facility, $24.8 million of hedge positions were secured under the credit agreement, and $52.4 million of letters of credit were issued and outstanding. At September 30, 2015, $100.0 million of the term loan was outstanding, no amount was outstanding under the revolving credit facility, $15.3 million of hedge positions were secured under the credit agreement, and $54.8 million of letters of credit were issued and outstanding.

At December 31, 2015, availability was $184.2 million, and the Partnership was in compliance with the fixed charge coverage ratio and the senior secured leverage ratio. At September 30, 2015, availability was $176.0 million, and the Partnership was in compliance with the fixed charge coverage ratio and the senior secured leverage ratio.

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10) Income Taxes

Since Star Gas Partners is organized as a master limited partnership, it is not subject to tax at its entity level for Federal and state income tax purposes. However, Star Gas Partners income is derived from its corporate subsidiaries, and these entities do incur Federal and state income taxes relating to their respective corporate subsidiaries, which are reflected in these financial statements. For the corporate subsidiaries of Star Gas Partners, a consolidated Federal income tax return is filed.

Income and losses of Star Gas Partners are allocated directly to the individual partners. Even though Star Gas Partners will generate non-qualifying Master Limited Partnership income through its corporate subsidiaries, cash received by Star Gas Partners from its corporate subsidiaries is generally included in the determination of qualified Master Limited Partnership income. All or a portion of such cash could be taxable as dividend income or as a capital gain to the individual partners. This could be the case even if Star Gas Partners used the cash received from its corporate subsidiaries for purposes such as the repurchase of Common Units, other types of capital transactions, or paying its own expenses rather than for distributions to its individual partners.

The accompanying financial statements are reported on a fiscal year, however, Star Gas Partners and its corporate subsidiaries file Federal and state income tax returns on a calendar year.

The current and deferred income tax expenses for the three months ended December 31, 2015, and 2014 are as follows:

(in thousands)	Three Months Ended December 31, 2015	2014
Income before income taxes	$ 21,475	$ 26,913
Current tax expense	$ 8,809	$ 11,129
Deferred tax expense	608	230
Total tax expense	$ 9,417	$ 11,359

As of January 1, 2016, Star Acquisitions, Inc., a wholly-owned subsidiary of the Partnership, had an estimated Federal net operating loss carry forward (NOLs) of approximately $3.9 million. The Federal NOLs, which will expire between 2018 and 2024, are generally available to offset any future taxable income but are also subject to annual limitations of between $1.0 million and $2.2 million.

Due to a change in a state tax law enacted in December 2015, the Partnership increased its valuation allowance by $0.5 million to a balance of $3.5 million at December 31, 2015.

At December 31, 2015, we did not have unrecognized income tax benefits.

Our continuing practice is to recognize interest and penalties related to income tax matters as a component of income tax expense. We file U.S. Federal income tax returns and various state and local returns. A number of years may elapse before an uncertain tax position is audited and finally resolved. For our Federal income tax returns we have four tax years subject to examination. In our major state tax jurisdictions of New York, Connecticut, Pennsylvania and New Jersey, we have four, four, four, and five tax years, respectively, that are subject to examination. While it is often difficult to predict the final outcome or the timing of resolution of any particular uncertain tax position, based on our assessment of many factors including past experience and interpretation of tax law, we believe that our provision for income taxes reflect the most probable outcome. This assessment relies on estimates and assumptions and may involve a series of complex judgments about future events.

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11) Supplemental Disclosure of Cash Flow Information

(in thousands)	Three Months Ended December 31, 2015	Three Months Ended December 31, 2014
Cash paid during the period for:		
Income taxes, net	$ 2,238	$ 11,116
Interest	$ 1,566	$ 6,233
Non-cash investing activities:		
Acquisition of NYC heating oil customer list	$	$ 886
Non-cash operating activities:		
Increase in interest expense amortization of debt discount on 8.875% Senior Notes and amortization of deferred charges on senior secured term loan	$ 71	$ 30

12) Commitments and Contingencies

The Partnership s operations are subject to the operating hazards and risks normally incidental to handling, storing and transporting and otherwise providing for use by consumers hazardous liquids such as home heating oil and propane. In the ordinary course of business the Partnership is a defendant in various legal proceedings and litigations. The Partnership records a liability when it is probable that a loss has been incurred and the amount is reasonably estimable. The Partnership maintains insurance policies with insurers in amounts and with coverages and deductibles we believe are reasonable and prudent. However, the Partnership cannot assure that this insurance will be adequate to protect it from all material expenses related to potential future claims. In the opinion of management the Partnership is not a party to any litigation which, individually or in the aggregate, could reasonably be expected to have a material adverse effect on the Partnership s results of operations, financial position or liquidity.

13) Earnings Per Limited Partner Unit

Income per limited partner unit is computed in accordance with FASB ASC 260-10-05 Earnings Per Share, Master Limited Partnerships (EITF 03-06), by dividing the limited partners interest in net income by the weighted average number of limited partner units outstanding. The pro forma nature of the allocation required by this standard provides that in any accounting period where the Partnership s aggregate net income exceeds its aggregate distribution for such period, the Partnership is required to present net income per limited partner unit as if all of the earnings for the periods were distributed, regardless of whether those earnings would actually be distributed during a particular period from an economic or practical perspective. This allocation does not impact the Partnership s overall net income or other financial results. However, for periods in which the Partnership s aggregate net income exceeds its aggregate distributions for such period, it will have the impact of reducing the earnings per limited partner unit, as the calculation according to this standard result in a theoretical increased allocation of undistributed earnings to the general partner. In accounting periods where aggregate net income does not exceed aggregate distributions for such period, this standard does not have any impact on the Partnership s net income per limited partner unit calculation. A separate and independent calculation for each quarter and year-to-date period is performed, in which the Partnership s contractual participation rights are taken into account.

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The following presents the net income allocation and per unit data using this method for the periods presented:

Basic and Diluted Earnings Per Limited Partner:	**Three Months Ended December 31,**	
(in thousands, except per unit data)	**2015**	**2014**
Net income	$ 12,058	$ 15,554
Less General Partner s interest in net income	68	88
Net income available to limited partners	11,990	15,466
Less dilutive impact of theoretical distribution of earnings under FASB ASC 260-10-45-60	1,231	1,930
Limited Partner s interest in net income under FASB ASC 260-10-45-60	$ 10,759	$ 13,536
Per unit data:		
Basic and diluted net income available to limited partners	$ 0.21	$ 0.27
Less dilutive impact of theoretical distribution of earnings under FASB ASC 260-10-45-60	0.02	