Sprague Resources LP
Form 10-Q
May 08, 2018
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 31, 2018
or
o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period to
Commission file number: 001-36137

Sprague Resources LP
(Exact name of registrant as specified in its charter)

Delaware	45-2637964
(State of incorporation)	(I.R.S. Employer Identification No.)

185 International Drive
Portsmouth, New Hampshire 03801
(Address of principal executive offices)
Registrant’s telephone number, including area code: (800) 225-1560
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 o
Indicated 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 Regulations S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer”, “smaller reporting company”, and "emerging growth company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer	o	Accelerated filer	x
Non-accelerated filer	o (Do not check if a smaller reporting company)	Smaller reporting company	o

Emerging growth company o
If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. o

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

The registrant had 22,727,284 common units outstanding as of May 1, 2018.

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Part I – FINANCIAL INFORMATION
Item 1 — Condensed Consolidated Financial Statements
Sprague Resources LP
Condensed Consolidated Balance Sheets
(in thousands except units)

	March 31, 2018 (Unaudited)	December 31, 2017
Assets		
Current assets:		
Cash and cash equivalents	$5,609	$6,815
Accounts receivable, net	281,459	316,613
Inventories	234,626	335,859
Fair value of derivative assets	53,438	107,254
Other current assets	27,449	39,946
Total current assets	602,581	806,487
Fair value of derivative assets long-term	18,718	7,493
Property, plant and equipment, net	349,045	350,059
Intangibles, net	68,764	71,891
Other assets, net	11,211	12,018
Goodwill	115,037	115,037
Total assets	$1,165,356	$1,362,985
Liabilities and unitholders' equity		
Current liabilities:		
Accounts payable	$90,708	$205,105
Accrued liabilities	47,058	49,038
Fair value of derivative liabilities	57,126	156,763
Due to General Partner	10,552	11,228
Current portion of working capital facilities	243,238	275,613
Current portion of other obligations	6,541	6,476
Total current liabilities	455,223	704,223
Commitments and contingencies		
Working capital facilities - less current portion	69,730	66,237
Acquisition facility	379,100	383,500
Fair value of derivative liabilities long-term	2,831	8,265
Other obligations - less current portion	49,314	49,625
Due to General Partner	1,795	1,678
Deferred income taxes	18,321	17,623
Total liabilities	976,314	1,231,151
Unitholders' equity:		
Common unitholders - public (10,620,936 units and 10,446,539 units issued and outstanding as of March 31, 2018 and December 31, 2017, respectively)	219,033	193,977
Common unitholders - affiliated (12,106,348 units issued and outstanding)	(22,700)	(53,273)
Accumulated other comprehensive loss, net of tax	(7,291)	(8,870)
Total unitholders' equity	189,042	131,834
Total liabilities and unitholders' equity	$1,165,356	$1,362,985

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

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Sprague Resources LP
Unaudited Condensed Consolidated Statements of Operations
(in thousands except unit and per unit amounts)

	Three Months Ended March 31,	
	2018	2017
Net sales	$1,331,148	$917,807
Cost of products sold (exclusive of depreciation and amortization)	1,183,982	795,146
Operating expenses	23,209	16,832
Selling, general and administrative	27,864	26,289
Depreciation and amortization	8,425	5,932
Total operating costs and expenses	1,243,480	844,199
Operating income	87,668	73,608
Other income	—	64
Interest income	112	84
Interest expense	(9,884)	(7,155)
Income before income taxes	77,896	66,601
Income tax provision	(2,975)	(2,102)
Net income	74,921	64,499
Incentive distributions declared	(1,714)	(742)
Limited partners' interest in net income	$73,207	$63,757
Net income per limited partner unit:		
Common - basic	$3.22	$2.98
Common - diluted	$3.21	$2.94
Units used to compute net income per limited partner unit:		
Common - basic	22,725,346	21,404,992
Common - diluted	22,786,889	21,718,627
Distribution declared per unit	$0.6525	$0.5925

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

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Sprague Resources LP
Unaudited Condensed Consolidated Statements of Comprehensive Income (Loss)
(in thousands)

	Three Months Ended March 31,	
	2018	2017
Net income	$74,921	$64,499
Other comprehensive income, net of tax:		
Unrealized gain on interest rate swaps		
Net gain arising in the period	1,941	301
Reclassification adjustment related to (gain) loss realized in income	(280)	120
Net change in unrealized gain on interest rate swaps	1,661	421
Tax effect	(13)	(6)
	1,648	415
Foreign currency translation adjustment	(69)	33
Other comprehensive income	1,579	448
Comprehensive income	$76,500	$64,947

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

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Sprague Resources LP
Unaudited Condensed Consolidated Statements of Unitholders' Equity (Deficit)
(in thousands)

	Common-Public	Common-Sprague Holdings	Subordinated-Sprague Holdings	Incentive Distribution Rights	Accumulated Other Comprehensive Loss	Total
Balance at December 31, 2016	$175,314	$(4,518)	$(34,576)	$ —	$(10,783)	$125,437
Conversion of subordinated units to common units	—	(40,393)	40,393	—	—	—
Net income	11,955	14,324	—	3,218	—	29,497
Other comprehensive income	—	—	—	—	1,913	1,913
Unit-based compensation	1,034	1,240	—	—	—	2,274
Distributions paid	(25,198)	(23,239)	(5,817)	(3,218)	—	(57,472)
Common units issued related to Carbo acquisition	31,401	—	—	—	—	31,401
Common units issued with annual bonus	161	210	—	—	—	371
Units withheld for employee tax obligations	(690)	(897)	—	—	—	(1,587)
Balance at December 31, 2017	$193,977	$(53,273)	$ —	$ —	$(8,870)	$131,834
Net income	34,367	39,181	—	1,373	—	74,921
Other comprehensive income	—	—	—	—	1,579	1,579
Unit-based compensation	392	446	—	—	—	838
Distributions paid	(8,531)	(7,718)	—	(1,373)	—	(17,622)
Units withheld for employee tax obligations	(1,172)	(1,336)	—	—	—	(2,508)
Balance at March 31, 2018	$219,033	$(22,700)	$ —	$ —	$(7,291)	$189,042

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

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Sprague Resources LP
Unaudited Condensed Consolidated Statements of Cash Flows
(in thousands)

	Three Months Ended March 31,	
	2018	2017
Cash flows from operating activities		
Net income	$74,921	$64,499
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization (includes amortization of deferred debt issuance costs)	9,307	6,947
Loss (gain) on sale of assets and insurance recoveries	19	(66)
Changes in fair value of contingent consideration	171	—
Provision for doubtful accounts	488	(17)
Non-cash unit-based compensation	838	859
Other	23	—
Deferred income taxes	607	1,263
Changes in assets and liabilities:		
Accounts receivable	34,666	25,505
Inventories	101,234	95,537
Other assets	12,503	11,636
Fair value of commodity derivative instruments	(60,820)	(43,878)
Due to General Partner and affiliates	(559)	(4,506)
Accounts payable, accrued liabilities and other	(116,663)	(52,367)
Net cash provided by operating activities	56,735	105,412
Cash flows from investing activities		
Purchases of property, plant and equipment	(3,681)	(7,176)
Business acquisitions	—	(58,910)
Proceeds from property insurance settlement and sale of assets	29	148
Net cash used in investing activities	(3,652)	(65,938)
Cash flows from financing activities		
Net borrowings (payments) under credit agreements	(33,021)	(11,743)
Payments on capital leases, term debt, and other obligations	(1,017)	(392)
Debt issue costs	(102)	(189)
Distributions to unitholders	(17,622)	(13,760)
Foreign exchange on capital lease obligations	(16)	—
Repurchased units withheld for employee tax obligations	(2,508)	(1,587)
Net cash used in financing activities	(54,286)	(27,671)
Effect of exchange rate changes on cash balances held in foreign currencies	(3)	21
Net change in cash and cash equivalents	(1,206)	11,824
Cash and cash equivalents, beginning of period	6,815	2,682
Cash and cash equivalents, end of period	$5,609	$14,506
Supplemental disclosure of cash flow information		
Cash paid for interest	$9,044	$5,933
Cash paid for taxes	$1,639	$922

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

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Sprague Resources LP
Notes to Unaudited Condensed Consolidated Financial Statements
(in thousands unless otherwise stated)

1. Description of Business and Summary of Significant Accounting Policies

Partnership Businesses

Sprague Resources LP (the “Partnership”) is a Delaware limited partnership formed on June 23, 2011 by Sprague Holdings and its General Partner and engages in the purchase, storage, distribution and sale of refined products and natural gas, and provides storage and handling services for a broad range of materials.

Unless the context otherwise requires, references to “Sprague Resources,” and the “Partnership,” refer to Sprague Resources LP and its subsidiaries. Unless the context otherwise requires, references to “Axel Johnson” or the “Parent” or the "Sponsor" refer to Axel Johnson Inc. and its controlled affiliates, collectively, other than Sprague Resources, its subsidiaries and its General Partner. References to “Sprague Holdings” refer to Sprague Resources Holdings LLC, a wholly owned subsidiary of Axel Johnson and the owner of the General Partner. References to the “General Partner” refer to Sprague Resources GP LLC.

The Partnership owns, operates and/or controls a network of refined products and materials handling terminals located in the Northeast United States and in Quebec, Canada. The Partnership also utilizes third-party terminals in the Northeast United States through which it sells or distributes refined products pursuant to rack, exchange and throughput agreements. The Partnership has four business segments: refined products, natural gas, materials handling and other operations.

- The refined products segment purchases a variety of refined products, such as heating oil, diesel fuel, residual fuel oil, kerosene, jet fuel, gasoline and asphalt (primarily from refining companies, trading organizations and producers), and sells them to wholesale and commercial customers.
- The natural gas segment purchases, sells and distributes natural gas to commercial and industrial customers. The Partnership purchases the natural gas it sells from natural gas producers and trading companies.
- The materials handling segment offloads, stores and prepares for delivery a variety of customer-owned products.
- The other operations segment includes the purchase and distribution of coal, certain commercial trucking activities and a heating equipment service business.

See Note 2 "Revenue" for a description of our revenue activities within these business segments.

Prior to February 16, 2017, Sprague Holdings owned, directly or indirectly, all of the Partnership’s subordinated units. The principal difference between the Partnership’s common units and subordinated units is that during the subordination period, the common units had the right to receive a minimum quarterly distribution of $0.4125 per common unit, plus any arrearages in the payment of the minimum quarterly distribution on the common units from prior quarters, before any distributions of cash from distributable cash flow may be made on the subordinated units. On February 16, 2017, based upon meeting certain distribution and performance tests provided in the Partnership's partnership agreement, all 10,071,970 subordinated units outstanding converted to common units on a one-for-one basis.

As of March 31, 2018, the Parent, through its ownership of Sprague Holdings, owned 12,106,348 common units representing 53% of the limited partner interest in the Partnership. Sprague Holdings also owns the General Partner, which in turn owns a non-economic interest in the Partnership. Sprague Holdings currently holds incentive distribution rights (“IDRs”) that entitle it to receive increasing percentages, up to a maximum of 50.0%, of the cash the Partnership distributes from distributable cash flow in excess of $0.474375 per unit per quarter. The maximum distribution of 50% does not include any distributions that Sprague Holdings may receive on any limited partner units that it owns. See Notes 12 and 13.

Basis of Presentation

The Condensed Consolidated Financial Statements include the accounts of the Partnership and its wholly-owned subsidiaries. Intercompany transactions between the Partnership and its subsidiaries have been eliminated. The accompanying unaudited Condensed Consolidated Financial Statements were prepared in accordance with the requirements of the Securities and Exchange Commission (“SEC”) for interim financial information. As permitted under

those rules, certain notes or other financial information that are normally required by U.S. generally accepted accounting principles ("GAAP") to be included in

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annual financial statements have been condensed or omitted from these interim financial statements. These interim financial statements should be read in conjunction with the consolidated financial statements and related notes of the Partnership’s Annual Report on Form 10-K for the year ended December 31, 2017 as filed with the SEC on March 14, 2018 (the “2017 Annual Report”).

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities in the balance sheet and the reported net sales and expenses in the income statement. Actual results could differ from those estimates. Among the estimates made by management are asset and liability valuations as part of an acquisition, the fair value of derivative assets and liabilities, valuation of contingent consideration, valuation of reporting units within the goodwill impairment assessment, and if necessary long-lived asset impairments and environmental and legal obligations.

The Condensed Consolidated Financial Statements included herein reflect all normal and recurring adjustments which, in the opinion of management, are necessary for a fair presentation of the Partnership’s consolidated financial position at March 31, 2018 and December 31, 2017, the consolidated results of operations for the three months ended March 31, 2018 and 2017, and the consolidated cash flows for the three months ended March 31, 2018 and 2017. The unaudited results of operations for the interim periods reported are not necessarily indicative of results to be expected for the full year. Demand for some of the Partnership’s refined petroleum products, specifically heating oil and residual oil for space heating purposes, and to a lesser extent natural gas, are generally higher during the first and fourth quarters of the calendar year which may result in significant fluctuations in the Partnership’s quarterly operating results.

Significant Accounting Policies

The Partnership's significant accounting policies are described in Note 1 “Description of Business and Summary of Significant Accounting Policies” in the Partnership’s audited consolidated financial statements included in the 2017 Annual Report and are the same as are used in preparing these unaudited interim Condensed Consolidated Financial Statements except for the adoption of ASU 2014-09, Revenue from Contracts with Customers (Topic 606) which the Partnership adopted as of January 1, 2018. The adoption of Topic 606 is discussed further in Recent Accounting Pronouncements below as well as in Note 2 "Revenue".

Recent Accounting Pronouncements

In July 2017, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2017-12, Derivatives and Hedging: Targeted Improvements to Accounting for Hedging Activities. The objective of the guidance is to improve the financial reporting of hedging relationships to better portray the economic results of an entity’s risk management activities in its financial statements. This ASU is effective for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. The Partnership is currently evaluating the impact of this new standard on the consolidated financial statements.

In January 2017, the FASB issued ASU 2017-04 Intangibles - Goodwill and Other (Topic 350): Simplifying the Accounting for Goodwill Impairment. The guidance removes Step 2 of the goodwill impairment test, which requires a hypothetical purchase price allocation. A goodwill impairment will now be the amount by which a reporting unit’s carrying value exceeds its fair value, not to exceed the carrying amount of goodwill. The standard will be applied prospectively, and is effective for fiscal years beginning after December 15, 2019. Early adoption is permitted for any impairment tests performed after January 1, 2017.

In January 2017, the FASB issued ASU 2017-01 Business Combinations (Topic 805), which clarifies the definition of a business with the objective of adding guidance to assist entities with evaluating whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses. This ASU is effective for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. The Partnership will consider this new guidance for transactions entered into after December 31, 2017.

In August 2016, the FASB issued ASU 2016-15 Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments, which addresses eight specific cash flow issues with the objective of reducing diversity in practice in how certain cash receipts and cash payments are presented and classified in the statement of cash flows under Topic 230, Statement of Cash Flows, and other Topics. This ASU is effective for fiscal years beginning after

December 15, 2017, and interim periods within those fiscal years and is to be applied retrospectively to all periods presented. The adoption of this guidance in 2018 did not have an impact on the Partnership's consolidated statements of cash flows.

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In February 2016, the FASB issued ASU 2016-02 Leases (Topic 842), which, among other things, requires lessees to recognize at the commencement date of a lease a liability, which is a lessee's obligation to make lease payments arising from a lease, measured on a discounted basis, and a right-of-use asset, which is an asset that represents the lessee's right to use, or control the use of, a specified asset for the lease term. This ASU is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early application is permitted. Lessees and lessors must apply a modified retrospective transition approach for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. The modified retrospective approach would not require any transition accounting for leases that expired before the earliest comparative period presented. Lessees and lessors may not apply a full retrospective transition approach. The Partnership is currently evaluating the impact of this new standard on the consolidated financial statements.
In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (Topic 606), which revises the principles of revenue recognition from one based on the transfer of risks and rewards to when a customer obtains control of a
good or service. The FASB issued several ASUs after ASU 2014-09 to clarify implementation guidance but did not change the core principle of the guidance in Topic 606. These ASUs are effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. The adoption of this standard in 2018 did not have an impact on the Partnership's consolidated financial statements nor result in significant changes to business processes, systems, or internal controls.

2. Revenue

Accounting Policies

Revenue is recognized when performance obligations under the terms of a contract with a customer are satisfied. The majority of the Partnership’s revenue is generated from refined products and natural gas contracts that have a single performance obligation which is the delivery of the related energy product. Accordingly, the Partnership recognizes revenue for refined products and natural gas when title and risk of loss have been transferred to the customer which is generally at the time of shipment or delivery of products. Revenue for the Partnership’s materials handling segment is recorded on a straight-line basis under leasing arrangements or as services are performed.

Revenue is measured as the amount of consideration the Partnership expects to receive in exchange for transferring products or providing services and is generally based upon a negotiated index, formula, list or fixed price. An allowance for doubtful accounts is recorded to reflect an estimate of the ultimate realization of the Partnership's accounts receivable and includes an assessment of the customers’ creditworthiness and the probability of collection. Estimated discounts are included in the transaction price of the contracts with customers as a reduction to net sales. The Partnership sells its products or provides its services directly to commercial customers and wholesale distributors generally under agreements with payment terms typically less than 30 days.

The Partnership has elected to account for shipping and handling as activities to fulfill the promise to transfer the good. As such, shipping and handling fees billed to customers in a sales transaction are recorded in net sales and shipping and handling costs incurred are recorded in cost of products sold (exclusive of depreciation and amortization). The Partnership has elected to exclude from net sales any value add, sales and other taxes which it collects concurrent with revenue-producing activities. These accounting policy elections are consistent with the way the Partnership historically recorded shipping and handling fees and taxes.

The majority of the Partnership's revenue is derived from contracts (i) with an original expected length of one year or less and (ii) contracts for which it recognizes revenue at the amount in which it has the right to invoice the customer as product is delivered. The Partnership has elected the practical expedient not to disclose the value of remaining performance obligations associated with these types of contracts.

Contract Balances

Contract liabilities primarily relate to advances or deposits received from the Partnership's customers before revenue is recognized. These amounts are included in accrued liabilities in the Condensed Consolidated Balance Sheets and amounted to $6.0 million and $7.7 million as of March 31, 2018 and December 31, 2017, respectively. A substantial portion of the contract liabilities as of December 31, 2017 remains outstanding as of March 31, 2018. The Partnership does not have any material contract assets as of March 31, 2018 or December 31, 2017.

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Disaggregated Revenue

In general, the Partnership's business segmentation is aligned according to the nature and economic characteristics of its products and customer relationships which provides meaningful disaggregation of each business segment's results of operations. The Partnership operates its businesses in the Northeast and Mid-Atlantic United States and Eastern Canada.

The refined products segment purchases a variety of refined products, such as heating oil, diesel fuel, residual fuel oil, kerosene, jet fuel, gasoline and asphalt (primarily from refining companies, trading organizations and producers), and sells them to wholesale and commercial customers. Refined products revenue-producing activities are direct sales to customers including throughput and exchange transactions. Revenue is recognized when the product is delivered. Revenue is not recognized on exchange agreements, which are entered into primarily to acquire refined products by taking delivery of products closer to the Partnership’s end markets. Net differentials or fees for exchange agreements are recorded within cost of products sold (exclusive of depreciation and amortization).

The natural gas segment purchases, sells and distributes natural gas to commercial and industrial customers. The Partnership purchases the natural gas it sells from natural gas producers and trading companies. Natural gas revenue-producing activities are sales to customers at various points on natural gas pipelines or at local distribution companies (i.e., utilities). Natural gas sales not billed by month-end are accrued based upon estimated gas volumes delivered.

The materials handling segment offloads, stores and prepares for delivery a variety of customer-owned products. A majority of the materials handling segment revenue is generated under leasing arrangements with revenue recorded over the lease term generally on a straight-line basis. Contingent rentals are recorded as revenue only when billable under the arrangement. For materials handling contracts that are not leases, the Partnership recognizes revenue either at a point in time as services are performed or over a period of time if the services are performed in a continuous fashion over the period of the contract.
The other operations segment includes the purchase and distribution of coal, certain commercial trucking activities and a heating equipment service business. Revenue from other activities is recognized when the product is delivered or the services are rendered.

Further disaggregation of net sales by business segment and geographic destination is as follows:

	Three Months Ended March 31,	
	2018	2017
Net sales:		
Refined products		
Distillates	$981,691	$630,753
Gasoline	76,357	69,694
Heavy fuel oil and asphalt	122,812	81,143
Total refined products	$1,180,860	$781,590
Natural gas	129,927	119,666
Materials handling	13,148	9,925
Other operations	7,213	6,626
Net sales	$1,331,148	$917,807
Net sales by Country:		
United States	$1,265,542	$871,575

Canada	65,606	46,232
Net sales	$1,331,148	$917,807

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3. Business Combinations
The Partnership completed five business acquisitions during the year ended December 31, 2017 as described below. Allocations of the purchase price to the assets acquired and liabilities assumed have been made to record, where applicable, inventory, derivative assets and liabilities, natural gas transportation assets and liabilities, property, plant and equipment, identifiable intangible assets such as customer relationships and non-compete agreements as well as goodwill. Proforma information relating to these acquisitions has not been presented because the impact on the Partnership's Condensed Consolidated Statement of Operations for the three months ended March 31, 2017 is not material.

The Partnership recognized $0.4 million and $0.3 million of acquisition related costs during the three months ended March 31, 2018 and 2017, respectively, which were expensed and are included in selling, general and administrative expense.

Year Ended December 31, 2017

Coen Energy

On October 1, 2017, the Partnership purchased the membership interests of Coen Energy, LLC and Coen Transport, LLC as well as assets consisting of four bulk plants and underlying real estate (collectively, "Coen Energy"). Coen Energy, located in Washington, PA, provides energy products to commercial and residential customers located in Pennsylvania, Ohio and West
Virginia. The Coen Energy business also provides energy fuel services to customers that are engaged in Marcellus and Utica
shale drilling operations. The Coen Energy business is supported by four in-land bulk plants, two throughput locations,
approximately 100 delivery vehicles and approximately 250 employees. Initial consideration paid was $35.3 million in cash, not including the purchase of inventory and other adjustments, which was financed with borrowings under our credit facility. Contingent consideration of up to $12 million is payable based on achieving certain economic performance measures during the three year period ending September 30, 2020. The operations of Coen Energy have been included in the Partnership's refined products segment since the acquisition date.

The following table summarizes the preliminary fair values of the assets acquired and liabilities assumed at the acquisition date:

Inventories	$567
Other current assets	115
Property, plant and equipment	12,972
Intangibles	18,375
Total identifiable assets acquired	32,029
Other liabilities	(256)
Net identifiable assets acquired	31,773
Goodwill	13,095
Net assets acquired	$44,868

The goodwill recognized is primarily attributable to Coen Energy's reputation in its geographic market area, the in-place workforce and the residual cash flow the Partnership believes that it will be able to generate. The goodwill is expected to be deductible for tax purposes.

Carbo Terminals

On April 18, 2017, the Partnership acquired substantially all of the assets of Carbo Industries, Inc. and certain of its affiliates (together "Carbo") by purchasing Carbo's Inwood and Lawrence, New York refined product terminal assets and its associated wholesale distribution business. The fair value of the consideration totaled $72.0 million and consisted of $13.3 million in cash that was financed through borrowings under the Credit Agreement, an obligation to pay $38.2 million over a ten year period (estimated net present value of $27.3 million) and $31.4 million in unregistered common units. The Carbo terminals have a combined gasoline, ethanol and distillate storage capacity of 174,000 barrels and are supplied primarily by pipeline with the ability to also accept product deliveries by barge and

truck. The operations of Carbo are included in the Partnership's refined products segment since the acquisition date.

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The following table summarizes the fair values of the assets acquired and liabilities assumed at the acquisition date:

Inventories	$3,220
Derivative and other current assets	111
Property, plant and equipment	22,995
Intangibles	29,000
Total identifiable assets acquired	55,326
Other liabilities	(188)
Net identifiable assets acquired	55,138
Goodwill	16,718
Net assets acquired	$71,856

The goodwill recognized is primarily attributable to Carbo’s reputation in the New York City area, the in-place workforce and the residual cash flow the Partnership believes that it will be able to generate. The goodwill is expected to be deductible for tax purposes.

Capital Terminal

On February 10, 2017, the Partnership purchased the East Providence, Rhode Island refined product terminal business of Capital Properties Inc. (the “Capital Terminal”). Consideration paid was $22.0 million and was financed with borrowings under the Credit Agreement. The terminal’s distillate storage capacity of 1.0 million barrels had been leased by the Partnership since April 2014 and was previously included in the Partnership’s total storage capacity. The operations of the Capital Terminal are included in the Partnership's refined products segment since the acquisition date.

The following table summarizes the fair values of the assets acquired and liabilities assumed at the acquisition date:

Property, plant and equipment	$21,960
Accrued liabilities and other, net	(22)
Net assets acquired	$21,938

Global Natural Gas & Power

On February 1, 2017, the Partnership purchased the natural gas marketing and electricity brokering business of Global Partners LP ("Global Natural Gas & Power") for $17.3 million, not including the purchase of natural gas inventory, assumption of derivative assets (liabilities) and other adjustments. Consideration paid was $16.3 million and was financed with borrowings under the Credit Agreement. This business markets natural gas and electricity to commercial, industrial, municipal and institutional customer locations in the Northeast United States. The operations of Global Natural Gas & Power are included in the Partnership's natural gas segment since the acquisition date.

The following table summarizes the fair values of the assets acquired and liabilities assumed at the acquisition date:

Inventory	$286
Derivative assets	5,873
Natural gas transportation assets	695
Derivative assets long term	1,089
Natural gas transportation assets long term	378
Intangibles	5,046
Total identifiable assets acquired	13,367
Derivative liabilities	(4,865)
Natural gas transportation liabilities	(465)
Derivative liabilities long term	(1,214)
Natural gas transportation liabilities long term	(162)
Net identifiable assets acquired	6,661
Goodwill	9,592

Net assets acquired	$16,253

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The goodwill recognized is primarily attributable to Global Natural Gas & Power's reputation in its market regions, the in-place workforce and the residual cash flow the Partnership believes that it will be able to generate. The goodwill is expected to be deductible for tax purposes.

L.E. Belcher Terminal

On February 1, 2017, the Partnership purchased the Springfield, Massachusetts refined product terminal assets of Leonard E. Belcher, Incorporated ("L.E. Belcher") for approximately $20.0 million, not including the purchase of inventory, assumption of derivative assets (liabilities) and other adjustments. Consideration paid was $20.7 million and was financed with borrowings under the Credit Agreement. The purchase consists of two pipeline-supplied distillate terminals and one distillate storage facility with a combined capacity of 283,000 barrels, as well as L.E. Belcher's associated wholesale and commercial fuels businesses. The operations of L.E. Belcher are included in the Partnership's refined products segment since the acquisition date.

The following table summarizes the fair values of the assets acquired and liabilities assumed at the acquisition date:

Inventories	$632
Derivative and other current assets	658
Property, plant and equipment	9,152
Intangibles	5,800
Total identifiable assets acquired	16,242
Derivative and other current liabilities	(680)
Net identifiable assets acquired	15,562
Goodwill	5,081
Net assets acquired	$20,643

The goodwill recognized is primarily attributable to L.E. Belcher's reputation in the Springfield, Massachusetts area, the in-place workforce and the residual cash flow the Partnership believes that it will be able to generate. The goodwill is expected to be deductible for tax purposes.

4. Accumulated Other Comprehensive Loss, Net of Tax

Amounts included in accumulated other comprehensive loss, net of tax, consisted of the following:

	March 31, 2018	December 31, 2017
Fair value of interest rate swaps, net of tax	$4,236	$2,588
Cumulative foreign currency translation adjustment	(11,527)	(11,458)
Accumulated other comprehensive loss, net of tax	$(7,291)	$(8,870)

5. Inventories

	March 31, 2018	December 31, 2017
Petroleum and related products	$226,649	$324,491
Asphalt	3,369	5,221
Coal	4,196	3,712
Natural gas	412	2,435
Inventories	$234,626	$335,859

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6. Credit Agreement

	March 31, 2018	December 31, 2017
Working capital facilities	$312,968	$341,850
Acquisition facility	379,100	383,500
Total credit agreement	692,068	725,350
Less: current portion of working capital facilities	(243,238)	(275,613)
Long-term portion	$448,830	$449,737

Sprague Operating Resources LLC and Kildair Service ULC ("Kildair"), wholly owned subsidiaries of the Partnership, are borrowers under an amended and restated revolving credit agreement that matures on April 27, 2021 (the "Credit Agreement"). Obligations under the Credit Agreement are secured by substantially all of the assets of the Partnership and its subsidiaries.

As of March 31, 2018, the revolving credit facilities under the Credit Agreement contained, among other items, the following:

- A U.S. dollar revolving working capital facility of up to $950.0 million, subject to borrowing base limits, to be used for working capital loans and letters of credit;
- A multicurrency revolving working capital facility of up to $100.0 million, subject to borrowing base limits, to be used for working capital loans and letters of credit;
- Revolving acquisition facility of up to $550.0 million, subject to acquisition facility borrowing base limits, to be used for loans and letters of credit to fund capital expenditures and acquisitions and other general corporate purposes related to the Partnership’s current businesses, and
- Subject to certain conditions including the receipt of additional commitments from lenders, the ability to increase the U.S. dollar revolving working capital facility by $250.0 million and the multicurrency revolving working capital facility by $220.0 million subject to a maximum combined increase for both facilities of $270.0 million in the aggregate. Additionally, subject to certain conditions, the revolving acquisition facility may be increased by $200.0 million.

Indebtedness under the Credit Agreement bears interest, at the borrowers’ option, at a rate per annum equal to either (i) the Eurocurrency Rate (which is the LIBOR Rate for loans denominated in U.S. dollars and CDOR for loans denominated in Canadian dollars, in each case adjusted for certain regulatory costs) for interest periods of one, two, three or six months plus a specified margin or (ii) an alternate rate plus a specified margin.

For loans denominated in U.S. dollars, the alternate rate is the Base Rate which is the highest of (a) the U.S. Prime Rate as in effect from time to time, (b) the greater of the Federal Funds Effective Rate and the Overnight Bank Funding Rate as in effect from time to time plus 0.50% and (c) the one-month Eurocurrency Rate for U.S. dollars as in effect from time to time plus 1.00%.

For loans denominated in Canadian dollars, the alternate rate is the Prime Rate which is the higher of (a) the Canadian Prime Rate as in effect from time to time and (b) the one-month Eurocurrency Rate for U.S. dollars as in effect from time to time plus 1.00%.

The working capital facilities are subject to borrowing base reporting and as of March 31, 2018 and December 31, 2017, had a borrowing base of $474.6 million and $623.2 million, respectively. As of March 31, 2018 and December 31, 2017, outstanding letters of credit were $24.6 million and $72.3 million, respectively. As of March 31, 2018, excess availability under the working capital facilities was $137.0 million and excess availability under the acquisition facilities was $170.9 million.

The weighted average interest rate was 4.5% and 4.2% at March 31, 2018 and December 31, 2017, respectively. No amounts are due under the Credit Agreement until the maturity date, however, the current portion of the Credit Agreement at March 31, 2018 and December 31, 2017 represents the amounts of the working capital facility intended to be repaid during the following twelve month period.

The Credit Agreement contains certain restrictions and covenants among which include a minimum level of net working capital, fixed charge coverage and debt leverage ratios and limitations on the incurrence of indebtedness. The Credit Agreement limits the Partnership’s ability to make distributions in the event of a default as defined in the Credit Agreement. As of March 31, 2018, the Partnership was in compliance with these covenants.

7. Related Party Transactions

The General Partner charges the Partnership for the reimbursements of employee costs and related employee benefits and other overhead costs supporting the Partnership’s operations which amounted to $35.0 million and $27.5 million for the three months ended March 31, 2018 and 2017, respectively. Through the General Partner, the Partnership also participates in the Parent’s pension and other post-retirement benefits. At March 31, 2018 and December 31, 2017, total amounts due to the General Partner with respect to these benefits and overhead costs were $12.3 million and $12.9 million, respectively.

8. Segment Reporting

The Partnership has four reporting segments that comprise the structure used by the chief operating decision makers (CEO and CFO/COO) to make key operating decisions and assess performance. When establishing a reporting segment, the Partnership aggregates individual operating units that are in the same line of business and have similar economic characteristics such as adjusted gross margin. These reporting segments are refined products, natural gas, materials handling and other activities.

The Partnership's refined products reporting segment purchases a variety of refined products, such as heating oil, diesel fuel, residual fuel oil, asphalt, kerosene, jet fuel and gasoline (primarily from refining companies, trading organizations and producers), and sells them to its customers. The Partnership has wholesale customers who resell the refined products they purchase from the Partnership and commercial customers who consume the refined products they purchase. The Partnership’s wholesale customers consist of home heating oil retailers and diesel fuel and gasoline resellers. The Partnership’s commercial customers include federal and state agencies, municipalities, regional transit authorities, drill sites, large industrial companies, real estate management companies, hospitals and educational institutions. The refined products reporting segment consists of three operating segments.

The Partnership's natural gas reporting segment purchases natural gas from natural gas producers and trading companies and sells and distributes natural gas to commercial and industrial customers primarily in the Northeast and Mid-Atlantic United States. The natural gas reporting segment consists of one operating segment.

The Partnership's materials handling reporting segment offloads, stores, and/or prepares for delivery a variety of customer-owned products, including asphalt, clay slurry, salt, gypsum, crude oil, residual fuel oil, coal, petroleum coke, caustic soda, tallow, pulp and heavy equipment. These services are generally provided under multi-year agreements as either fee-based activities or as leasing arrangements when the right to use an identified asset (such as storage tanks or storage locations) has been conveyed in the agreement. The materials handling reporting segment consists of two operating segments.

The Partnership's other reporting segment includes the purchase, sale and distribution of coal, commercial trucking activities unrelated to its refined products segment and a heating equipment service business. Other activities are not reported separately as they represent less than 10% of consolidated net sales and adjusted gross margin. The other activities reporting segment consists of two operating segments.

The Partnership evaluates segment performance based on adjusted gross margin, a non-GAAP measure, which is net sales less cost of products sold (exclusive of depreciation and amortization) increased by unrealized hedging losses and decreased by unrealized hedging gains, in each case with respect to refined products and natural gas inventory, prepaid forward contracts and natural gas transportation contracts.

Based on the way the business is managed, it is not reasonably possible for the Partnership to allocate the components of operating costs and expenses among the operating segments. There were no significant intersegment sales for any of the years presented below.

The Partnership had no single customer that accounted for more than 10% of total net sales for the three months ended March 31, 2018 and 2017, respectively. The Partnership’s foreign sales, primarily sales of refined products, asphalt and natural gas to its customers in Canada, were $65.6 million and $46.2 million for the three months ended March 31,

2018 and 2017, respectively.

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	Three Months Ended March 31,	
	2018	2017
Net sales:		
Refined products	$1,180,860	$781,590
Natural gas	129,927	119,666
Materials handling	13,148	9,925
Other operations	7,213	6,626
Net sales	$1,331,148	$917,807
Adjusted gross margin (1):		
Refined products	$56,335	$39,478
Natural gas	37,948	38,590
Materials handling	13,148	9,925
Other operations	2,106	2,373
Adjusted gross margin	109,537	90,366
Reconciliation to operating income (loss) (2):		
Add: unrealized gain (loss) on inventory derivatives (3)	23,561	24,508
Add: unrealized gain on prepaid forward contract derivatives (4)	—	(27)
Add: unrealized (loss) gain on natural gas transportation contracts (5)	14,068	7,814
Operating costs and expenses not allocated to operating segments:		
Operating expenses	(23,209)	(16,832)
Selling, general and administrative	(27,864)	(26,289)
Depreciation and amortization	(8,425)	(5,932)
Operating income	87,668	73,608
Other income	—	64
Interest income	112	84
Interest expense	(9,884)	(7,155)
Income tax provision	(2,975)	(2,102)
Net income	$74,921	$64,499

(1) The Partnership trades, purchases, stores and sells energy commodities that experience market value fluctuations. To manage the Partnership's underlying performance, including its physical and derivative positions, management utilizes adjusted gross margin, which is a non-GAAP financial measure. Adjusted gross margin is also used by external users of the Partnership's consolidated financial statements to assess the Partnership's economic results of operations and its commodity market value reporting to lenders. In determining adjusted gross margin, the Partnership adjusts its segment results for the impact of unrealized hedging gains and losses with regard to refined products and natural gas inventory derivatives, prepaid forward contract derivatives and natural gas transportation contracts, which are not marked to market for the purpose of recording unrealized gains or losses in net income. These adjustments align the unrealized hedging gains and losses to the period in which the revenue from the sale of inventory, prepaid fixed forwards and the utilization of transportation contracts relating to those hedges is realized in net income. Adjusted gross margin has no impact on reported volumes or net sales.

(2) Reconciliation of adjusted gross margin to operating income, the most directly comparable GAAP measure.

(3) Inventory is valued at the lower of cost or net realizable value. The fair value of the derivatives the Partnership uses to economically hedge its inventory declines or appreciates in value as the value of the underlying inventory appreciates or declines, which creates unrealized hedging losses (gains) with respect to the derivatives that are included in net income.

(4)

The unrealized hedging gain (loss) on prepaid forward contract derivatives represents the Partnership's estimate of the change in fair value of the prepaid forward contracts which are not recorded in net income until the forward contract is settled in the future (i.e., when the commodity is delivered to the customer). As these contracts are prepaid, they do not qualify as derivatives and changes in the fair value are therefore not included in net income. The fair value of the derivatives the Partnership uses to economically hedge its prepaid forward contracts declines or appreciates in value as the value of the underlying prepaid forward contract appreciates or declines, which creates unrealized hedging gains (losses) that are included in net income.

(5) The unrealized hedging gain (loss) on natural gas transportation contracts represents the Partnership's estimate of the change in fair value of the natural gas transportation contracts which are not recorded in net income until the transportation is utilized in the future (i.e., when natural gas is delivered to the customer), as these contracts do not qualify as derivatives. As the fair value of the natural gas transportation contracts decline or appreciate, the offsetting physical or financial derivative will also appreciate or decline creating unmatched unrealized hedging (losses) gains in net income as of each period end.

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Segment Assets

Due to the commingled nature and uses of the Partnership's fixed assets, the Partnership does not track its fixed assets between its refined products and materials handling operating segments or its other activities. There are no significant fixed assets attributable to the natural gas reportable segment.

At March 31, 2018, goodwill recorded for the refined products, natural gas, materials handling and other operations segments amounted to $71.4 million, $35.5 million, $6.9 million and $1.2 million, respectively.

9. Financial Instruments and Off-Balance Sheet Risk

As of March 31, 2018 and December 31, 2017, the carrying amounts of cash, cash equivalents and accounts receivable approximated fair value because of the short maturity of these instruments. As of March 31, 2018 and December 31, 2017, the carrying value of the Partnership's margin deposits with brokers approximates fair value and consists of initial margin with futures transaction brokers, along with variation margin, which is paid or received on a daily basis, and is included in other current assets. As of March 31, 2018 and December 31, 2017, the carrying value of the Partnership's debt approximated fair value due to the variable interest nature of these instruments.

The Partnership's deferred consideration was recorded in connection with an acquisition on April 18, 2017 using an estimated fair value discount at the time of the transaction. As of March 31, 2018, the carrying value of the deferred consideration approximated fair value due to the fact that there has been no significant subsequent change in the estimated fair value discount rate.

The following table presents financial assets and financial liabilities of the Partnership measured at fair value on a recurring basis:

	As of March 31, 2018			
	Fair Value Measurement	Quoted Prices in Active Markets Level 1	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3
Derivative assets:				
Commodity fixed forwards	$31,566	$4	$ 31,562	$ —
Commodity swaps and options	35,952	35,947	5	—
Commodity derivatives	67,518	35,951	31,567	—
Interest rate swaps	4,638	—	4,638	—
Total derivative assets	$72,156	$35,951	$ 36,205	$ —
Derivative liabilities:				
Commodity fixed forwards	$15,012	$—	$ 15,012	$ —
Commodity swaps and options	44,573	44,509	64	—
Commodity derivatives	59,585	44,509	15,076	—
Interest rate swaps	369	—	369	—
Other	3	—	3	—
Total derivative liabilities	$59,957	$44,509	$ 15,448	$ —
Contingent consideration	$9,896	$—	$ —	$ 9,896

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	As of December 31, 2017			
	Fair Value Measurement	Quoted Prices in Active Markets Level 1	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3
Derivative assets:				
Commodity fixed forwards	$11,502	$—	$ 11,502	$ —
Commodity swaps and options	100,630	100,613	17	—
Commodity derivatives	112,132	100,613	11,519	—
Interest rate swaps	2,615	—	2,615	—
Total derivatives assets	$114,747	$100,613	$ 14,134	$ —
Derivative liabilities:				
Commodity fixed forwards	$61,195	$—	$ 61,195	$ —
Commodity swaps and options	103,827	103,654	173	—
Commodity derivatives	165,022	103,654	61,368	—
Interest rate swaps	6	—	6	—
Total derivative liabilities	$165,028	$103,654	$ 61,374	$ —
Contingent consideration	$9,725	$—	$ —	$ 9,725

Derivative Instruments

The Partnership utilizes derivative instruments consisting of futures contracts, forward contracts, swaps, options and other derivatives individually or in combination, to mitigate its exposure to fluctuations in prices of refined petroleum products and natural gas. The use of these derivative instruments within the Partnership's risk management policy may generate gains or losses from changes in market prices. The Partnership enters into futures and over-the-counter (“OTC”) transactions either on regulated exchanges or in the OTC market. Futures contracts are exchange-traded contractual commitments to either receive or deliver a standard amount or value of a commodity at a specified future date and price, with some futures contracts based on cash settlement rather than a delivery requirement. Futures exchanges typically require margin deposits as security. OTC contracts, which may or may not require margin deposits as security, involve parties that have agreed either to exchange cash payments or deliver or receive the underlying commodity at a specified future date and price. The Partnership posts initial margin with futures transaction brokers, along with variation margin, which is paid or received on a daily basis, and is included in other current assets. In addition, the Partnership may either pay or receive margin based upon exposure with counterparties. Payments made by the Partnership are included in other current assets, whereas payments received by the Partnership are included in accrued liabilities. Substantially all of the Partnership’s commodity derivative contracts outstanding as of March 31, 2018 will settle prior to September 30, 2019.

The Partnership enters into some master netting arrangements to mitigate credit risk with significant counterparties. Master netting arrangements are standardized contracts that govern all specified transactions with the same counterparty and allow the Partnership to terminate all contracts upon occurrence of certain events, such as a counterparty’s default. The Partnership has elected not to offset the fair value of its derivatives, even where these arrangements provide the right to do so.

The Partnership’s derivative instruments are recorded at fair value, with changes in fair value recognized in net income (loss) each period. The Partnership’s fair value measurements are determined using the market approach and includes non-performance risk and time value of money considerations. Counterparty credit is considered for receivable balances, and the Partnership’s credit is considered for payable balances.

The Partnership determines fair value using a hierarchy for the inputs used to measure the fair value of financial assets and liabilities based on the source of the input, which generally range from quoted prices for identical instruments in a principal trading market (Level 1) to estimates determined using significant unobservable inputs (Level 3). Multiple

inputs may be used to measure fair value; however, the level of fair value is based on the lowest significant input level within this fair value hierarchy.

Details on the methods and assumptions used to determine the fair values are as follows:

Fair value measurements based on Level 1 inputs: Measurements that are most observable and are based on quoted prices of identical instruments obtained from the principal markets in which they are traded. Closing prices are both readily available and representative of fair value. Market transactions occur with sufficient frequency and volume to assure liquidity.

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Fair value measurements based on Level 2 inputs: Measurements derived indirectly from observable inputs or from quoted prices from markets that are less liquid are considered Level 2. Measurements based on Level 2 inputs include OTC derivative instruments that are priced on an exchange traded curve, but have contractual terms that are not identical to exchange traded contracts. The Partnership utilizes fair value measurements based on Level 2 inputs for its fixed forward contracts, over-the-counter commodity price swaps, interest rate swaps and forward currency contracts.
Fair value measurements based on Level 3 inputs: Measurements that are least observable are estimated from significant unobservable inputs determined from sources with little or no market activity for comparable contracts or for positions with longer durations. The Partnership utilizes fair value measurements based on Level 3 inputs for its contingent consideration liability.
The Partnership does not offset fair value amounts recognized for the right to reclaim cash collateral (a receivable) or the obligation to return cash collateral (a payable) against the fair value of derivative instruments executed with the same counterparty under the same master netting arrangement. The Partnership had no right to reclaim or obligation to return cash collateral as of March 31, 2018 and December 31, 2017.

The Partnership enters into derivative contracts with counterparties, some of which are subject to master netting arrangements, which allow net settlements under certain conditions. The Partnership presents derivatives at gross fair values in the Condensed Consolidated Balance Sheets. The maximum amount of loss due to credit risk that the Partnership would incur if its counterparties failed completely to perform according to the terms of the contracts, based on the net fair value of these financial instruments, exclusive of cash collateral, was $35.7 million at March 31, 2018. Information related to these offsetting arrangements is set forth below:

	As of March 31, 2018					
				Gross Amount Not Offset in the Balance Sheet		
	Gross Amount of Recognized Assets/ Liabilities	Gross Amount Offset in the Balance Sheet	Amount of Assets/ Liabilities in the Balance Sheet	Financial Instruments	Cash Collateral Posted	Net Amount
Commodity derivative assets	$67,518	$ —	$ 67,518	$ (36,480)	$ —	$ 31,038
Interest rate swap derivative assets	4,638	—	4,638	—	—	4,638
Fair value of derivative assets	$72,156	$ —	$ 72,156	$ (36,480)	$ —	$ 35,676
Commodity derivative liabilities	$(59,585)	$ —	$ (59,585)	$ 36,480	$ 8,739	$ (14,366)
Interest rate swap derivative liabilities	(369)	—	(369)	—	—	(369)
Other	(3)		(3)			(3)
Fair value of derivative liabilities	$(59,957)	$ —	$ (59,957)	$ 36,480	$ 8,739	$ (14,738)

As