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HERITAGE PROPANE PARTNERS L P

Form 10-Q/A

November 26, 2003

FORM 10-Q/A

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

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

FOR THE QUARTERLY PERIOD ENDED NOVEMBER 30, 2002

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES  
EXCHANGE ACT OF 1934

FOR THE TRANSITION PERIOD FROM \_\_\_\_\_ to

COMMISSION FILE NUMBER 1-11727

HERITAGE PROPANE PARTNERS, L.P.

(Exact name of registrant as specified in its charter)

DELAWARE

73-1493906

(state or other jurisdiction or  
incorporation or organization)

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

8801 SOUTH YALE AVENUE, SUITE 310

TULSA, OKLAHOMA 74137

(Address of principal  
executive offices  
and zip code)

(918)492-7272

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

At January 13, 2003, the registrant had units outstanding as follows:

Heritage Propane Partners, L.P. 16,367,803 Common Units

EXPLANATORY NOTE

We are filing this Amendment on Form 10-Q/A in conjunction with the filing of a Registration Statement on Form S-3 (File No. 333-107324). That Registration Statement incorporates our quarterly report on Form 10-Q for the quarterly period ended November 30, 2003, originally filed on January 14, 2003 (the "Original Filing"). This Form 10-Q/A amends and restates in its entirety

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our quarterly report on Form 10-Q for the quarterly period ended November 30, 2003.

This Amendment makes certain changes in the form of additional or supplemental disclosures as follows:

- Part I--Item 1. Financial Information and Notes to Consolidated Financial Statements, pages 2-16: As described in Note 2 to the Consolidated Financial Statements, we have revised our previously reported Consolidated Statements of Operations for the three months ended November 30, 2003 and 2002 and have made corresponding revisions to the Notes to Consolidated Financial Statements to make the presentations required by EITF 02-3. This information was previously shown in the Consolidated Statements of Operations on a gross basis in the separately presented line items of "Revenues-liquids marketing", "Revenues--other" and "Costs and expenses--liquids marketing", and is now presented on a net basis in a single line item as "Liquids marketing, net". The revisions had no effect on previously reported Operating Income or Net Income. In addition, we have provided additional and supplemental information regarding (i) the recording (loss) of the minority interests of all partially owned subsidiaries, (ii) a description of our Costs and Expenses, (iii) quarterly distributions, (iv) Heritage's buying and selling of derivative financial instruments and liquids marketing contracts, and (v) our adoption of EITF 02-3.
- We have revised our previously reported Consolidated Balance Sheet as of November 30, 2002 and the related Consolidated Statements of Operations, Other Comprehensive Income (Loss), Partners' Capital, and Cash Flows for the three months ended November 30, 2002 and have made corresponding revisions to the Notes to Consolidated Financial Statements to reflect the adoption of the fair value recognition provisions of Statement of Financial Accounting Standards No. 123 Accounting for Stock-based Compensation (SFAS 123) effective as of September 1, 2002. During the fourth quarter of 2003, Heritage adopted the fair value recognition provisions following the modified prospective method of adoption described in Statement of Financial Accounting Standards No. 148, Accounting for Stock-Based Compensation - Transition and Disclosure (SFAS 148). Following adoption, deferred compensation expense that is recognized will be the same as that which would have been recognized had the fair value recognition provisions of SFAS 123 been applied to all awards granted under the Restricted Unit Plan and the Long Term Incentive Plan granted after its original effective date. Results from prior years have not been restated. It was our decision to adopt this preferable method of accounting for our stock-based employee compensation plans, as we believe it provides a better measurement of our compensation costs.
- Part I--Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations, pages 19-22: We have revised to provide additional or supplemental disclosures about results of operations, the terms of our credit agreements and our long-term debt and other contractual obligations, our adoption of EITF 02-3, the recording of the minority interests of all partially owned subsidiaries and Heritage's buying and selling of derivative financial instruments. Additionally, we have retitled "EBITDA" as

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"EBITDA, as adjusted" and made clarifications regarding how we calculate EBITDA, as adjusted. These revisions did not change how we calculate EBITDA, as adjusted, and it is calculated in the same manner as we have historically presented such information.

- Part I--Item 3. Quantitative and Qualitative Disclosure about Market Risk, pages 23-25: We have provided additional or supplemental disclosures about Heritage's buying and selling of derivative financial instruments and liquids marketing contracts,

This report continues to speak as of the date of the Original Filing, and we have not updated the disclosure in this report to speak as of a later date. All information contained in this report and the Original Filing is subject to updating and supplementing as provided in our periodic reports filed with the Securities and Exchange Commission.

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HERITAGE PROPANE PARTNERS, L.P.

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PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

HERITAGE PROPANE PARTNERS, L.P. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS  
(in thousands, except unit data)  
(unaudited)

	November 30, 2002	August 31, 2002
	-----	-----
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	\$ 5,223	\$ 4,596
Marketable securities	2,559	2,559
Accounts receivable, net of allowance for doubtful accounts	57,619	30,898
Inventories	53,267	48,187
Assets from liquids marketing	813	2,301
Prepaid expenses and other	8,451	6,846
	-----	-----
Total current assets	127,932	95,387
PROPERTY, PLANT AND EQUIPMENT, net	402,567	400,044
INVESTMENT IN AFFILIATES	8,072	7,858
GOODWILL, net of amortization prior to adoption of SFAS No. 142	156,258	155,735
INTANGIBLES AND OTHER ASSETS, net	56,491	58,240
	-----	-----
Total assets	\$ 751,320	\$ 717,264
	=====	=====
LIABILITIES AND PARTNERS' CAPITAL		
CURRENT LIABILITIES:		
Working capital facility	\$ 52,800	\$ 30,200
Accounts payable	56,903	40,929
Accounts payable to related companies	4,558	5,002
Accrued and other current liabilities	28,505	23,962
Liabilities from liquids marketing	772	1,818
Current maturities of long-term debt	22,628	20,158
	-----	-----
Total current liabilities	166,166	122,069
LONG-TERM DEBT, less current maturities	418,607	420,021
MINORITY INTERESTS	3,528	3,564
	-----	-----

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Total liabilities	588,301	545,654
	-----	-----
COMMITMENTS AND CONTINGENCIES		
PARTNERS' CAPITAL:		
Common Unitholders (15,816,347 and 15,815,847 units issued and outstanding at November 30, 2002 and August 31, 2002, respectively)	165,175	173,677
Class C Unitholders (1,000,000 units issued and outstanding at November 30, 2002 and August 31, 2002)	-	-
General Partner	1,496	1,585
Accumulated other comprehensive loss	(3,652)	(3,652)
	-----	-----
Total partners' capital	163,019	171,610
	-----	-----
Total liabilities and partners' capital	\$ 751,320	\$ 717,264
	=====	=====

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

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HERITAGE PROPANE PARTNERS, L.P. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS  
(in thousands, except per unit and unit data)  
(unaudited)

	Three Months Ended November 30,	
	2002	2001
	-----	-----
REVENUES:		
Retail fuel	\$ 84,050	\$ 83,200
Wholesale fuel	11,348	12,593
Liquids marketing, net	707	(3,325)
Other	17,355	15,490
	-----	-----
Total revenues	113,460	107,958
	-----	-----
COSTS AND EXPENSES:		
Cost of products sold	57,020	60,235
Operating expenses	33,392	31,844
Depreciation and amortization	9,266	9,058
Selling, general and administrative	2,856	2,951
	-----	-----
Total costs and expenses	102,534	104,088
	-----	-----
OPERATING INCOME	10,926	3,870

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OTHER INCOME (EXPENSE):		
Interest expense	(9,297)	(9,216)
Equity in earnings of affiliates	213	129
Gain on disposal of assets	67	467
Other	(278)	(98)
	-----	-----
INCOME (LOSS) BEFORE MINORITY INTERESTS	1,631	(4,848)
Minority interests	(127)	69
	-----	-----
NET INCOME (LOSS)	1,504	(4,779)
GENERAL PARTNER'S INTEREST IN NET INCOME (LOSS)	233	168
	-----	-----
LIMITED PARTNERS' INTEREST IN NET INCOME (LOSS)	\$ 1,271	\$ (4,947)
	=====	=====
BASIC NET INCOME (LOSS) PER LIMITED PARTNER UNIT	\$ 0.08	\$ (0.32)
	=====	=====
BASIC AVERAGE NUMBER OF UNITS OUTSTANDING	15,816,347	15,644,580
	=====	=====
DILUTED NET INCOME (LOSS) PER LIMITED PARTNER UNIT	\$ 0.08	\$ (0.32)
	=====	=====
DILUTED AVERAGE NUMBER OF UNITS OUTSTANDING	15,848,698	15,644,580
	=====	=====

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

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HERITAGE PROPANE PARTNERS, L.P. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)  
(in thousands, unaudited)

	Three Months Ended November 30,	
	2002	2001
	-----	-----
Net income (loss)	\$ 1,504	\$ (4,779)
Other comprehensive income (loss)		
Reclassification adjustment for losses or gains on derivative instruments included in net income	-	(2,755)
Change in value of available-for-sale securities	-	377
	-----	-----

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Comprehensive income (loss)	\$ 1,504	\$ (7,157)
	=====	=====
RECONCILIATION OF ACCUMULATED OTHER COMPREHENSIVE LOSS		
Balance, beginning of period	\$ (3,652)	\$ (6,541)
Current period reclassification to earnings	-	1,590
Current period change	-	(2,378)
	-----	-----
Balance, end of period	\$ (3,652)	\$ (7,329)
	=====	=====

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

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HERITAGE PROPANE PARTNERS, L.P. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF PARTNERS' CAPITAL  
(in thousands, except unit data)  
(unaudited)

	Number of Units		Common	Class C	General Partner
	Common	Class C			
BALANCE, AUGUST 31, 2002	15,815,847	1,000,000	\$ 173,677	\$ -	\$ 1,585
Unit distribution	-	-	(10,082)	-	(322)
Conversion of phantom units	500	-	-	-	-
Other	-	-	309	-	-
Net change in accumulated other comprehensive income per accompanying statements	-	-	-	-	-
Net income	-	-	1,271	-	233
	-----	-----	-----	-----	-----
BALANCE, NOVEMBER 30, 2002	15,816,347	1,000,000	\$ 165,175	\$ -	\$ 1,496
	=====	=====	=====	=====	=====

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

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## HERITAGE PROPANE PARTNERS, L.P. AND SUBSIDIARIES

### CONSOLIDATED STATEMENTS OF CASH FLOWS (in thousands) (unaudited)

	Three Months Ended November 30,	
	2002	2001
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net income (loss)	\$ 1,504	\$ (4,77
Reconciliation of net income (loss) to net cash provided by (used in) operating activities-		
Depreciation and amortization	9,266	9,05
Provision for loss on accounts receivable	234	35
Gain on disposal of assets	(67)	(46
Deferred compensation on restricted units and long-term incentive plan	309	48
Undistributed earnings of affiliates	(213)	(14
Minority interests	(36)	(21
Changes in assets and liabilities, net of effect of acquisitions:		
Accounts receivable	(26,887)	(17,50
Inventories	(4,938)	(13,29
Assets from liquids marketing	1,488	(34
Prepaid and other expenses	(1,558)	8,80
Intangibles and other assets	(64)	(18
Accounts payable	15,830	17,08
Accounts payable to related companies	(444)	1,66
Accrued and other current liabilities	4,280	(2,62
Liabilities from liquids marketing	(1,046)	2,20
	(2,342)	8
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Cash paid for acquisitions, net of cash acquired	(1,603)	(7,34
Capital expenditures	(9,652)	(9,79
Proceeds from the sale of assets	1,491	1,11
	(9,764)	(16,02
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Proceeds from borrowings	48,750	56,26
Principal payments on debt	(25,613)	(27,67
Unit distributions	(10,404)	(10,05
Other	-	(4
	12,733	18,48
<b>INCREASE IN CASH AND CASH EQUIVALENTS</b>		
	627	2,55
CASH AND CASH EQUIVALENTS, beginning of period	4,596	5,62

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CASH AND CASH EQUIVALENTS, end of period	\$ 5,223	\$ 8,17
	=====	=====
NONCASH FINANCING ACTIVITIES:		
Notes payable incurred on noncompete agreements	\$ 519	\$ 16
	=====	=====
SUPPLEMENTAL DISCLOSURE OF CASH FLOW		
INFORMATION:		
Cash paid during the period for interest	\$ 7,247	\$ 7,74
	=====	=====

The accompanying notes are an integral part of these financial statements

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### HERITAGE PROPANE PARTNERS, L.P. AND SUBSIDIARIES

#### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollar amounts in thousands, except unit and per unit data)  
(unaudited)

#### 1. OPERATIONS AND ORGANIZATION:

The accompanying financial statements should be read in conjunction with the consolidated financial statements of Heritage Propane Partners, L.P. and subsidiaries (the "Partnership") as of August 31, 2002, and the notes thereto included in the Partnership's consolidated financial statements included in Form 10-K as filed with the Securities and Exchange Commission on November 27, 2002. The accompanying financial statements include only normal recurring accruals and all adjustments that the Partnership considers necessary for a fair presentation. Due to the seasonal nature of the Partnership's business, the results of operations for interim periods are not necessarily indicative of the results to be expected for a full year.

In order to simplify the Partnership's obligations under the laws of several jurisdictions in which it conducts business, the Partnership's activities are conducted through a subsidiary operating partnership, Heritage Operating, L.P. (the "Operating Partnership"). The Partnership and the Operating Partnership are collectively referred to in this report as "Heritage." At November 30, 2002, the Operating Partnership sold propane and propane-related products to more than 600,000 active residential, commercial, industrial, and agricultural customers in 28 states. Heritage is also a wholesale propane supplier in the southwestern and southeastern United States and in Canada, the latter through participation in MP Energy Partnership. MP Energy Partnership is a Canadian partnership, in which Heritage owns a 60% interest, engaged in supplying Heritage's northern U.S. locations and lower-margin wholesale distribution. Heritage buys and sells financial instruments for its own account through its wholly owned subsidiary, Heritage Energy Resources L.L.C. ("Resources").

#### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND BALANCE SHEET DETAIL:

##### PRINCIPLES OF CONSOLIDATION

The consolidated financial statements of the Partnership include the accounts of its subsidiaries, including the Operating Partnership, MP Energy Partnership, Heritage Service Corp., Guilford Gas Service, Inc., and Resources. A minority interest liability and minority interest expense is recorded for all partially owned subsidiaries. Heritage accounts for its 50% partnership interest in Bi-State Propane, a propane retailer in the states of Nevada and California, under the equity method. All significant intercompany transactions and accounts have been eliminated in consolidation. For purposes of maintaining partner

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capital accounts, the Partnership Agreement of Heritage Propane Partners, L.P. specifies that items of income and loss shall be allocated among the partners in accordance with their percentage interests. Normal allocations according to percentage interests are made, however, only after giving effect to any priority income allocations in an amount equal to the incentive distributions that are allocated 100% to the General Partner. On February 4, 2002, at a special meeting of the Partnership's Common Unitholders, the Common Unitholders approved the substitution of U.S. Propane, L.P. ("U.S. Propane") as the successor General Partner of the Partnership and the Operating Partnership, replacing Heritage Holdings, Inc. ("Heritage Holdings"). At November 30, 2002, U.S. Propane's 1.0101% general partner interest in the Operating Partnership was accounted for in the consolidated financial statements as a minority interest. For the three months ended November 30, 2001, the 1.0101% general partner interest of the former General Partner, Heritage Holdings, and U.S. Propane's 1.0101% limited partner interest in the Operating Partnership were accounted for in the consolidated financial statements as minority interests.

### REVENUE RECOGNITION

Sales of propane, propane appliances, parts, and fittings are recognized at the later of the time of delivery of the product to the customer or the time of sale or installation. Revenue from service labor is recognized upon completion of the service and tank rent is recognized ratably over the period it is earned. The Partnership does not separately charge shipping and handling costs to customers.

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### COSTS AND EXPENSES

Costs of products sold include actual cost of fuel sold adjusted for the effects of qualifying cash flow hedges, storage fees and inbound freight, and the cost of appliances, parts, and fittings. Operating expenses include all costs incurred to provide products to customers, including compensation for operations personnel, insurance costs, vehicle maintenance, advertising costs, shipping and handling costs, purchasing costs, and plant operations. Selling, general and administrative expenses include all corporate expenses and compensation for corporate personnel.

### ACCOUNTS RECEIVABLE

Heritage grants credit to its customers for the purchase of propane and propane-related products. Accounts receivable consisted of the following:

	November 30, 2002	August 31, 2002
	-----	-----
Accounts receivable	\$ 60,129	\$ 33,402
Less - allowance for doubtful accounts	2,510	2,504
	-----	-----
Total, net	\$ 57,619	\$ 30,898
	=====	=====

The activity in the allowance for doubtful accounts consisted of the following:

For the three months ended

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	November 30, 2002	November 30, 2001
Balance, beginning of the period	\$ 2,504	\$ 3,576
Provision for loss on accounts receivable	234	350
Accounts receivable written off, net of recoveries	(228)	(359)
Balance, end of period	\$ 2,510	\$ 3,567

INVENTORIES

Inventories are valued at the lower of cost or market. The cost of fuel inventories is determined using weighted-average cost of fuel delivered to the customer service locations and includes storage fees and inbound freight costs, while the cost of appliances, parts, and fittings is determined by the first-in, first-out method. Inventories consisted of the following:

	November 30, 2002	August 31, 2002
Fuel	\$ 43,751	\$ 38,523
Appliances, parts and fittings	9,516	9,664
Total inventories	\$ 53,267	\$ 48,187

RECLASSIFICATIONS

Certain prior period amounts have been reclassified to conform with the November 30, 2002 presentation. These reclassifications have no impact on net income or net assets.

INCOME (LOSS) PER LIMITED PARTNER UNIT

Basic net income (loss) per limited partner unit is computed by dividing net income (loss), after considering the General Partner's interest, by the weighted average number of Common Units outstanding. Diluted net income (loss) per limited partner unit is computed by dividing net income, after considering the General Partner's interest, by the weighted average number of Common Units outstanding and the weighted average number of restricted units

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("Phantom Units") granted under the Restricted Unit Plan. A reconciliation of net income (loss) and weighted average units used in computing basic and diluted net income (loss) per unit is as follows:

Three Months Ended  
November 30,

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	2002 ----	2001 ----
BASIC NET INCOME (LOSS) PER LIMITED PARTNER UNIT:		
Limited Partners' interest in net income (loss)	\$ 1,271	\$ (4,947)
	-----	-----
Weighted average limited partner units	15,816,347	15,644,580
	=====	=====
Basic net income (loss) per limited partner unit	\$ 0.08	\$ (0.32)
	=====	=====

	Three Months Ended November 30,	
	2002 ----	2001 ----
DILUTED NET INCOME (LOSS) PER LIMITED PARTNER UNIT:		
Limited partners' interest in net income (loss)	\$ 1,271	\$ (4,947)
	=====	=====
Weighted average limited partner units	15,816,347	15,644,580
Dilutive effect of phantom units (a)	32,351	-
	-----	-----
Weighted average limited partner units, assuming dilutive effect of phantom units	15,848,698	15,644,580
	=====	=====
Diluted net income (loss) per limited partner unit	\$ 0.08	\$ (0.32)
	=====	=====

(a) For the three months ended November 30, 2001, 41,900 phantom units were excluded from the calculation of diluted net loss as such units were anti-dilutive due to the net loss for the period.

QUARTERLY DISTRIBUTIONS OF AVAILABLE CASH

The Partnership Agreement requires that the Partnership will distribute all of its Available Cash to its Unitholders and its General Partner within 45 days following the end of each fiscal quarter, subject to the payment of incentive distributions to the holders of Incentive Distribution Rights to the extent that certain target levels of cash distributions are achieved. The term Available Cash generally means, with respect to any fiscal quarter of the Partnership, all cash on hand at the end of such quarter, plus working capital borrowings after the end of the quarter, less reserves established by the General Partner in its sole discretion to provide for the proper conduct of the Partnership's business, to comply with applicable laws or any debt instrument or other agreement, or to provide funds for future distributions to partners with respect to any one or more of the next four quarters. Available Cash is more fully defined in the Partnership Agreement.

Prior to the Special Meeting on February 4, 2002, distributions by the Partnership in an amount equal to 100% of Available Cash were made 97% to the Common Unitholders, 1.0101% to U.S. Propane for its limited partner interest in the Operating Partnership, and 1.9899% to the former General Partner, Heritage Holdings. After the approval by the Common Unitholders of the substitution of

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U.S. Propane as the General Partner, distributions by the Partnership in an amount equal to 100% of Available Cash will generally be made 98% to the Common Unitholders and 2% to the General Partner, subject to the payment of incentive distributions to the holders of Incentive Distribution Rights to the extent that certain target levels of cash distributions are achieved.

On October 15, 2002, a quarterly distribution of \$0.6375 per unit, or \$2.55 annually, was paid to Unitholders of record at the close of business on October 8, 2002 and to the General Partner for its general partner interest in the Partnership, its minority interest, and its Incentive Distribution Rights. On December 18, 2002, the Partnership declared a cash distribution for the first quarter ended November 30, 2002 of \$0.6375 per unit, or \$2.55 per unit annually, payable on January 14, 2003 to Unitholders of record at the close of business on December 30, 2002. These quarterly distributions include incentive distributions payable to the General Partner to the extent the quarterly distribution exceeds \$0.55 per unit. The total amount of distributions for the first quarter ended November 30, 2002 on Common Units, the general partner interests and the Incentive Distribution Rights totaled \$10.1 million, \$0.2 million and \$0.2 million, respectively. All such distributions were made from Available Cash from Operating Surplus.

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### STOCK BASED COMPENSATION PLANS

During the fourth quarter of 2003, Heritage adopted the fair value recognition provisions of Statement of Financial Accounting Standards No. 123 Accounting for Stock-based Compensation (SFAS 123) effective as of September 1, 2002. Heritage adopted the fair value recognition provisions following the modified prospective method of adoption described in Statement of Financial Accounting Standards No. 148, Accounting for Stock-Based Compensation - Transition and Disclosure (SFAS 148). Following adoption, deferred compensation expense that is recognized in the financial statements will be the same as that which would have been recognized had the fair value recognition provisions of SFAS 123 been applied to all awards under the Restricted Unit Plan and the Long Term Incentive Plan granted after October 1, 1995.

### RESTRICTED UNIT PLAN

The General Partner has adopted the Amended and Restated Restricted Unit Plan dated August 10, 2000, amended February 4, 2002 as the Second Amended and Restated Restricted Unit Plan (the "Restricted Unit Plan"), for certain directors and key employees of the General Partner and its affiliates. The Restricted Unit Plan covers rights to acquire 146,000 Common Units. The right to acquire the Common Units under the Restricted Unit Plan, including any forfeiture or lapse of rights is available for grant to key employees on such terms and conditions (including vesting conditions) as the Compensation Committee of the General Partner shall determine. Each director shall automatically receive a Director's grant with respect to 500 Common Units on each September 1 that such person continues as a director. Newly elected directors are also entitled to receive a grant with respect to 2,000 Common Units upon election or appointment to the Board. Directors who are employees of U.S. Propane, TECO, Atmos Energy, Piedmont Natural Gas or AGL Resources or their affiliates are not entitled to receive a Director's grant of Common Units. Generally, the rights to acquire the Common Units will vest upon the later to occur of (i) the three-year anniversary of the grant date, or on such terms as the Compensation Committee may establish, which may include the achievement of performance objectives. In the event of a "change of control" (as defined in the Restricted Unit Plan), all rights to acquire Common Units pursuant to the Restricted Unit Plan will immediately vest.

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The issuance of the Common Units pursuant to the Restricted Unit Plan is intended to serve as a means of incentive compensation for performance and not primarily as an opportunity to participate in the equity appreciation in respect of the Common Units. Therefore, no consideration will be payable by the plan participants upon vesting and issuance of the Common Units. As of November 30, 2002, 41,400 restricted units were outstanding and 15,800 were available for grants to non-employee directors and key employees.

Deferred compensation expense of \$81 was recognized for the three months ended November 30, 2002. For the three months ended November 30, 2001, Heritage followed the disclosure only provisions of SFAS 123, as amended by SFAS 148 and APB Opinion No. 25 Accounting for Stock Issued to Employees (APB 25). Under APB 25, the Restricted Unit Plan was classified as a variable plan so that an estimate of compensation was required based on a combination of the fair market value of the Common Units as of the end of the reporting period and an assessment of meeting certain performance criteria. Deferred compensation expense of \$98 was recognized for three months ended November 30, 2001 on the units based on the fair value of such units at the end of the period.

### LONG-TERM INCENTIVE PLAN

Effective September 1, 2000, Heritage adopted a long-term incentive plan whereby Common Units will be awarded based on achieving certain targeted levels of Distributed Cash (as defined in the Long Term Incentive Plan) per unit. Awards under the program will be made starting in 2003 based upon the average of the prior three years' Distributed Cash per unit. A minimum of 250,000 Common Units and if certain targeted levels are achieved, a maximum of 500,000 Common Units will be awarded.

Deferred compensation expense on this plan of \$228 was recognized for the three months ended November 30, 2002. For the three months ended November 30, 2001, Heritage followed the disclosure only provisions of SFAS 123, as amended by SFAS 148, and APB 25. Under APB 25, the Long Term Incentive Plan was classified as a variable plan so that an estimate of compensation was required based on a combination of the fair market value of the Common Units as of the end of the reporting period and an assessment of meeting certain performance criteria. Deferred compensation expense on this plan of \$389 was recognized for the three months ended November 30, 2001 based on the fair value of such units at the end of the period. The expense was determined based on the Partnership achieving the minimum award available under the plan.

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SFAS 123 requires that significant assumptions be used during the year to estimate the fair value, which includes the risk-free interest rate used, the expected life of the grants under each of the plans, the expected volatility, and the expected distributions on each of the grants. Heritage assumed a weighted average risk free interest rate of 5.72% for the three months ended November 30, 2002 and 5.90% for the three months ended November 20, 2001 in estimating the present value of the future cash flows of the distributions during the vesting period on the measurement date of each grant. Annual average cash distributions at the grant date were estimated to be \$2.39 for the three months ended November 30, 2002, and \$2.47 for the three months ended November 30, 2001. The expected life of each grant is assumed to be the minimum vesting period under certain performance criteria of each grant. The following table illustrates the effect on limited partners' interest in net income (loss) and the basic and diluted net income (loss) per limited partner unit if Heritage had applied the fair value recognition provisions of SFAS 123 to the Restricted Unit Plan and the Long-Term Incentive Plan for all periods presented.

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NET INCOME (LOSS) PER LIMITED  
PARTNER UNIT:

	November 30, 2002	2001
	-----	-----
Limited partners' interest in net income (loss)	\$ 1,271	\$
Add: Deferred compensation expense net of General Partner's and minority interest included in limited partners' interest in net income (loss)	304	
Deduct: Deferred compensation expense net of General Partner's and minority interest determined under the fair value based method	(304)	
	-----	-----
Pro forma limited partners' interest in net income (loss)	\$ 1,271	\$
	=====	=====
Weighted average limited partner units	15,816,347	15,6
	=====	=====
Basic net income (loss) per limited partner unit as reported	\$ 0.08	\$
	=====	=====
Basic net income (loss) per limited partner unit pro forma	\$ 0.08	\$
	=====	=====
Weighted average limited partner units, assuming dilutive effect of Phantom Units	15,848,698	15,6
	=====	=====
Diluted net income (loss) per limited partner unit as reported	\$ 0.08	\$
	=====	=====
Diluted net income (loss) per limited partner unit proforma	\$ 0.08	\$
	=====	=====

As stated above, during the fourth quarter of 2003, Heritage adopted the fair value recognition provisions of Statement of Financial Accounting Standards No. 123 Accounting for Stock-based Compensation (SFAS 123) effective as of September 1, 2002. Accordingly, the following information compares the originally reported consolidated statement of operations, reclassified for the adoption of EITF 02-3 for the three months ended November 30, 2002 and as adjusted for the adoption of SFAS 123:

	As originally reported	As adjusted for the adoption of SFAS 123
REVENUES:		
Retail fuel	\$ 84,050	\$ 84,050
Wholesale fuel	11,348	11,348
Liquids marketing, net	707	707
Other	17,355	17,355
	-----	-----

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Total revenues	113,460	113,460
	-----	-----
COSTS AND EXPENSES:		
Cost of products sold	57,020	57,020
Operating expenses	33,425	33,392
Depreciation and amortization	9,266	9,266
Selling, general and administrative	3,192	2,856
	-----	-----
Total costs and expenses	102,903	102,534
	-----	-----
OPERATING INCOME	10,557	10,926
OTHER INCOME (EXPENSE):		
Interest expense	(9,297)	(9,297)
Equity in earnings of affiliates	213	213
Gain on disposal of assets	67	67
Other	(278)	(278)
	-----	-----
INCOME (LOSS) BEFORE MINORITY INTERESTS	1,262	1,631
Minority interests	(123)	(127)
	-----	-----
NET INCOME (LOSS)	1,139	1,504
GENERAL PARTNER'S INTEREST IN NET INCOME (LOSS)	229	233
	-----	-----
LIMITED PARTNERS' INTEREST IN NET INCOME (LOSS)	\$ 910	\$ 1,271
	=====	=====
BASIC NET INCOME (LOSS) PER LIMITED PARTNER UNIT	\$ 0.06	\$ 0.08
	=====	=====
BASIC AVERAGE NUMBER OF UNITS OUTSTANDING	15,816,347	15,816,347
	=====	=====
DILUTED NET INCOME (LOSS) PER LIMITED PARTNER UNIT	\$ 0.06	\$ 0.08
	=====	=====
DILUTED AVERAGE NUMBER OF UNITS OUTSTANDING	15,848,698	15,848,698
	=====	=====

ACCOUNTING FOR DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES

Heritage applies Financial Accounting Standards Board ("FASB") Statement No. 133, Accounting for Derivative Instruments and Hedging Activities (SFAS 133). SFAS 133 requires that all derivatives be recognized in the balance sheet as either an asset or liability measured at fair value. Special accounting for

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qualifying hedges allows a derivative's gains and losses to offset related results on the hedged item in the statement of operations. During the three months ended November 30, 2001, Heritage reclassified into earnings through cost of products sold, a loss of \$1,590 that was previously reported in accumulated other comprehensive loss. There were no such financial instruments outstanding as of November 30, 2002.

### RECENTLY ISSUED ACCOUNTING STANDARDS

In June 2001, the FASB issued Statement No. 143, Accounting for Asset Retirement Obligations (SFAS 143). SFAS 143 addresses financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. This statement requires that the fair value of a liability for an asset retirement obligation be recognized in the period in which it is incurred if a reasonable estimate of fair value can be made. The associated asset retirement costs are capitalized as part of the carrying amount of the long-lived asset. Heritage adopted the provisions of SFAS 143 on September 1, 2002. The adoption of SFAS 143 did not have a material impact on the Partnership's consolidated financial position or results of operations.

In August 2001, the FASB issued Statement No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets (SFAS 144). SFAS 144 supersedes FASB Statement No. 121, Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of (SFAS 121), and the accounting and reporting provisions of APB Opinion No. 30, Reporting the Results of Operations - Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions. SFAS 144 retains the fundamental provisions of SFAS 121 for recognition and measurement of the impairment of long-lived assets to be held and used, and measurement of long-lived assets to be disposed of by sale. Heritage adopted the provisions of SFAS 144 on September 1, 2002. The adoption of SFAS 144 did not have a material impact on the Partnership's consolidated financial position or results of operations.

In April 2002, the FASB issued Statement No. 145, Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections (SFAS 145). SFAS 145 rescinds FASB Statement No. 4, Reporting Gains and Losses from Extinguishment of Debt, and an amendment of that Statement, FASB Statement No. 64, Extinguishments of Debt Made to Satisfy Sinking-Fund Requirements. SFAS 145 also rescinds FASB

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Statement No. 44, Accounting for Intangible Assets of Motor Carriers, amends FASB Statement No. 13, Accounting for Leases, to eliminate an inconsistency between the required accounting for sale-leaseback transactions and the required accounting for certain lease modifications that have economic effects that are similar to sale-leaseback transactions and also amends other existing authoritative pronouncements to make various technical corrections, clarify meanings, or describe their applicability under changed conditions. Heritage adopted the provisions of SFAS 145 on September 1, 2002. The adoption did not have a material impact on the Partnership's consolidated financial position or results of operations.

In October 2002, the EITF of the FASB discussed EITF Issue No. 02-3, Issues Related to Accounting for Contracts Involved in Energy Trading and Risk Management Activities (EITF 02-3). The EITF reached a consensus to rescind EITF Issue No. 98-10, Accounting for Contracts Involved in Energy Trading and Risk Management Activities (EITF 98-10), the impact of which is to preclude mark-to-market accounting for energy trading contracts not within the scope of

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SFAS 133. The EITF also reached a consensus that gains and losses on derivative instruments within the scope of SFAS 133 should be shown net in the statement of operations if the derivative instruments are held for trading purposes and what the disclosure requirements should be. This consensus was effective for financial statements issued for periods ending after July 15, 2002. Heritage adopted EITF 02-3 as of August 31, 2002, and upon application reclassified comparative financial statements for prior periods to conform to the consensus. This adoption did not have a material impact on Heritage's financial position or results of operations. The consensus regarding the rescission of EITF 98-10 is applicable for fiscal periods beginning after December 15, 2002. Energy trading contracts not within the scope of SFAS 133 purchased after October 25, 2002, but prior to the implementation of the consensus are not permitted to apply mark-to-market accounting. The adoption of EITF 02-3 as it relates to the rescission of EITF 98-10 is not expected to have a material impact on Heritage's financial position or results of operations.

The adoption of EITF 02-3 requires that realized and unrealized gains and losses be shown net for all periods presented. The following table summarizes the amounts that have been reclassified in the statement of operations:

	For the Three Months Ended	
	November 30,	
	2002	2001
	-----	-----
Revenue - liquids marketing	\$ 60,730	\$ 50,820
Costs and expenses - liquids marketing	(60,023)	(54,145)
	-----	-----
Net, as reclassified	\$ 707	\$ (3,325)
	=====	=====

In June 2002, the FASB issued Statement No. 146, Accounting for Costs Associated with Exit or Disposal Activities (SFAS 146). SFAS 146 addresses financial accounting and reporting for costs associated with exit or disposal activities and requires that a liability for a cost associated with an exit or disposal activity be recognized and measured initially at fair value only when the liability is incurred. Heritage adopted the provisions of SFAS 146 effective for exit or disposal activities that are initiated after December 31, 2002. The adoption did not have a material impact on the Partnership's consolidated financial position or results of operations.

In November 2002, the FASB issued Financial Interpretation No. 45 "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others" (FIN 45). FIN 45 expands the existing disclosure requirements for guarantees and requires that companies recognize a liability for guarantees issued after December 31, 2002. The implementation of FIN 45 did not have a significant impact on Heritage's financial position or results of operations.

### RECENTLY ISSUED ACCOUNTING STANDARDS NOT YET ADOPTED

In April 2003, the FASB issued Statement No. 149, Amendment of Statement 133 on Derivative Instruments and Hedging Activities (SFAS 149). SFAS 149 amends and clarifies financial accounting and reporting for derivative instruments embedded in other contracts (collectively referred to as derivatives) and for hedging activities under SFAS 133. SFAS 149 is effective for contracts entered into or modified after June 30, 2003, and for hedging relationships designated after June 30, 2003. Management does not believe that the adoption will have a material impact on the Partnership's consolidated financial position or results

of operations.

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In May 2003, the FASB issued Statement No. 150, Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity (SFAS 150). SFAS 150 establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. It requires that an issuer classify a financial instrument that is within the scope of SFAS 150 as a liability (or an asset in some circumstances). This statement is effective for financial instruments entered into or modified after May 31, 2003, and otherwise is effective at the beginning of the first interim period beginning after June 15, 2003. Management does not believe that the adoption will have a material impact on the Partnership's consolidated financial position or results of operations.

3. WORKING CAPITAL FACILITY AND LONG-TERM DEBT:

Effective July 16, 2001, the Operating Partnership entered into the Fifth Amendment to the First Amended and Restated Credit Agreement. The terms of the Agreement as amended are as follows:

A \$65,000 Senior Revolving Working Capital Facility is available through June 30, 2004. The interest rate and interest payment dates vary depending on the terms Heritage agrees to when the money is borrowed. Heritage must be free of all working capital borrowings for 30 consecutive days each fiscal year. The weighted average interest rate was 3.255% for the amount outstanding at November 30, 2002. The maximum commitment fee payable on the unused portion of the facility is 0.50%. All receivables, contracts, equipment, inventory, general intangibles, cash concentration accounts, and the capital stock of Heritage's subsidiaries secure the Senior Revolving Working Capital Facility. As of November 30, 2002, the Senior Revolving Working Capital Facility had a balance outstanding of \$52,800.

A \$50,000 Senior Revolving Acquisition Facility is available through December 31, 2003, at which time the outstanding amount must be paid in ten equal quarterly installments beginning March 31, 2004. The interest rate and interest payment dates vary depending on the terms Heritage agrees to when the money is borrowed. The weighted average interest rate was 3.255% for the amount outstanding at November 30, 2002. The maximum commitment fee payable on the unused portion of the facility is 0.50%. All receivables, contracts, equipment, inventory, general intangibles, cash concentration accounts, and the capital stock of Heritage's subsidiaries secure the Senior Revolving Acquisition Facility. As of November 30, 2002, the Senior Revolving Acquisition Facility had a balance outstanding of \$15,300.

4. REPORTABLE SEGMENTS:

The Partnership's financial statements reflect four reportable segments: the domestic retail operations of Heritage, the domestic wholesale operations of Heritage, the foreign wholesale operations of MP Energy Partnership, and the liquids marketing activities of Resources. Heritage's reportable domestic and wholesale fuel segments are strategic business units that sell products and services to retail and wholesale customers. Intersegment sales by the foreign wholesale segment to the domestic segment are priced in accordance with the partnership agreement of MP Energy Partnership. Heritage manages these segments separately as each segment involves different distribution, sale, and marketing strategies. Heritage evaluates the performance of its operating segments based

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on operating income, exclusive of selling, general, and administrative expenses of \$2,856 and \$2,951 for the three months ended November 30, 2002 and 2001, respectively. Selling, general and administrative expenses, interest expense and other expenses are not allocated by segment. Investment in affiliates and equity in earnings (losses) of affiliates relates primarily to Heritage's investment in Bi-State Propane (see Note 6), and is part of the domestic retail fuel segment. The following table presents the unaudited financial information by segment for the following periods:

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	For the Three Months ended November 30,	
	2002	2001
	-----	-----
<b>Gallons:</b>		
Domestic retail fuel	76,721	74,790
Domestic wholesale fuel	4,890	4,997
Foreign wholesale fuel		
Affiliated	20,380	15,071
Unaffiliated	17,195	18,264
Elimination	(20,380)	(15,071)
	-----	-----
Total	98,806	98,051
	=====	=====
<b>Revenues:</b>		
Domestic retail fuel	\$ 84,050	\$ 83,200
Domestic wholesale fuel	2,411	3,071
Foreign wholesale fuel		
Affiliated	10,408	8,940
Unaffiliated	8,937	9,522
Elimination	(10,408)	(8,940)
Liquids marketing, net	707	(3,325)
Other	17,355	15,490
	-----	-----
Total	\$ 113,460	\$ 107,958
	=====	=====
<b>Operating Income (Loss):</b>		
Domestic retail	\$ 13,437	\$ 10,523
Domestic wholesale fuel	(484)	(635)
Foreign wholesale fuel		
Affiliated	110	-
Unaffiliated	506	338
Elimination	(110)	-
Liquids marketing	323	(3,405)
	-----	-----
Total	\$ 13,782	\$ 6,821
	=====	=====
<b>Gain on Disposal of Assets:</b>		
Domestic retail fuel	\$ 80	\$ 216
Domestic wholesale fuel	(13)	251
	-----	-----
Total	\$ 67	\$ 467
	=====	=====

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	=====	=====
Minority Interest Expense:		
Corporate	\$          16	\$         (99)
Foreign wholesale	111	30
	-----	-----
Total	\$         127	\$         (69)
	=====	=====

Depreciation and amortization:		
Domestic retail	\$      9,132	\$      8,989
Domestic wholesale	129	64
Foreign wholesale	5	5
	-----	-----
Total	\$      9,266	\$      9,058
	=====	=====

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	As of November 30, 2002	As of August 31, 2002
	-----	-----
Total Assets:		
Domestic retail	\$     694,665	\$     667,978
Domestic wholesale	14,891	14,372
Foreign wholesale	10,135	10,564
Liquids Marketing	16,169	6,919
Corporate	15,460	17,431
	-----	-----
Total	\$     751,320	\$     717,264
	=====	=====
Additions to property, plant and equipment including acquisitions:		
Domestic retail fuel	\$     10,995	\$     39,904
Domestic wholesale	38	-
Foreign wholesale	-	46
Corporate	143	1,441
	-----	-----
Total	\$     11,176	\$     41,391
	=====	=====

Corporate assets include vehicles, office equipment and computer software for the use of administrative personnel. These assets are not allocated to segments. Corporate minority interest expense relates to U.S. Propane's general partner interest in the Operating Partnership.

5. SUBSEQUENT EVENT:

On January 2, 2003, the Partnership completed the acquisition of the propane assets of V-1 Oil Co. ("V-1") of Idaho Falls, Idaho. Under the terms of the acquisition, the Operating Partnership acquired all of the propane distribution assets of V-1 for a total consideration of approximately \$32.3 million, after adjustments. The acquisition price was payable \$17.3 million in cash, financed

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by the Acquisition Facility, and by the issuance of 551,456 Common Units of the Registrant valued at \$15.0 million. The exchange price for the Common Units was \$27.20, determined under a formula based upon the average closing price of the Registrant's Common Units for the twenty (20) consecutive trading days commencing on the tenth trading day prior to the public announcement of the transaction on December 10, 2002.

### 6. SIGNIFICANT INVESTEE:

Heritage holds a 50% interest in Bi-State Propane. Heritage accounts for this 50% interest in Bi-State Propane under the equity method. Heritage's investment in Bi-State Propane totaled \$7,691 and \$7,485 at November 30, 2002 and August 31, 2002 respectively. Heritage did not receive any distributions from Bi-State Propane for the three months ended November 30, 2002 or 2001. On March 1, 2002, the Operating Partnership sold certain assets acquired in the ProFlame acquisition to Bi-State Propane for approximately \$9,730 plus working capital. This sale was made pursuant to the provision in the Bi-State Propane partnership agreement that requires each partner to offer to sell any newly acquired businesses within Bi-State Propane's area of operations to Bi-State Propane. In conjunction with this sale, the Operating Partnership guaranteed \$5 million of debt incurred by Bi-State Propane to a financial institution. Based on the current financial condition of Bi-State Propane, management considers the likelihood of Heritage incurring a liability resulting from the guarantee to be remote. Heritage has not recorded a liability on the balance sheets as of November 30, 2002 or August 31, 2002 for this guarantee because the guarantee was in effect prior to the issuance of FIN 45, and there have been no amendments to the original guarantee. Bi-State Propane's financial position is summarized below:

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	November 30, 2002	August 31, 2002
	-----	-----
Current assets	\$ 3,776	\$ 3,321
Noncurrent assets	22,701	23,105
	-----	-----
	\$ 26,477	\$ 26,426
	=====	=====
Current liabilities	\$ 2,974	\$ 3,344
Long-term debt	9,450	9,450
Partners' capital:		
Heritage	7,691	7,485
Other partner	6,362	6,147
	-----	-----
	\$ 26,477	\$ 26,426
	=====	=====

Bi-State Propane's results of operations for the three months ended November 30, 2002 and 2001, respectively are summarized below:

For the Three Months Ended  
November 30,

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	2002	2001
Revenues	\$ 4,641	\$ 2,860
Gross profit	2,285	1,455
Net income:		
Heritage	206	126
Other Partner	215	143

### ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Heritage Propane Partners, L.P. (the "Registrant" or "Partnership"), is a Delaware limited partnership. The Partnership's common units are listed on the New York Stock Exchange. The Partnership's business activities are primarily conducted through its subsidiary, Heritage Operating, L.P. (the "Operating Partnership"), a Delaware limited partnership. The Partnership is the sole limited partner of the Operating Partnership, with a 98.9899% limited partner interest. The Partnership and the Operating Partnership are sometimes referred to collectively in this report as "Heritage."

The following is a discussion of the historical financial condition and results of operations of the Partnership and its subsidiaries, and should be read in conjunction with the Partnership's historical consolidated financial statements and accompanying notes thereto included elsewhere in this Quarterly Report on Form 10-Q.

#### FORWARD-LOOKING STATEMENTS

CERTAIN MATTERS DISCUSSED IN THIS REPORT, EXCLUDING HISTORICAL INFORMATION, AS WELL AS SOME STATEMENTS BY HERITAGE IN PERIODIC PRESS RELEASES AND SOME ORAL STATEMENTS OF HERITAGE OFFICIALS DURING PRESENTATIONS ABOUT THE PARTNERSHIP, INCLUDE CERTAIN "FORWARD-LOOKING" STATEMENTS WITHIN THE MEANING OF SECTION 27A OF THE SECURITIES ACT OF 1933 AND SECTION 21E OF THE SECURITIES EXCHANGE ACT OF 1934. STATEMENTS USING WORDS SUCH AS "ANTICIPATE," "BELIEVE," "INTEND," "PROJECT," "PLAN," "CONTINUE," "ESTIMATE," "FORECAST," "MAY," "WILL," OR SIMILAR EXPRESSIONS HELP IDENTIFY FORWARD-LOOKING STATEMENTS. ALTHOUGH HERITAGE BELIEVES SUCH FORWARD-LOOKING STATEMENTS ARE BASED ON REASONABLE ASSUMPTIONS AND CURRENT EXPECTATIONS AND PROJECTIONS ABOUT FUTURE EVENTS, NO ASSURANCE CAN BE GIVEN THAT EVERY OBJECTIVE WILL BE REACHED.

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ACTUAL RESULTS MAY DIFFER MATERIALLY FROM ANY RESULTS PROJECTED, FORECASTED, ESTIMATED, OR EXPRESSED IN FORWARD-LOOKING STATEMENTS SINCE MANY OF THE FACTORS THAT DETERMINE THESE RESULTS ARE DIFFICULT TO PREDICT AND ARE BEYOND MANAGEMENT'S CONTROL. SUCH FACTORS INCLUDE:

- CHANGES IN GENERAL ECONOMIC CONDITIONS IN THE UNITED STATES OF AMERICA AS WELL AS CHANGES IN GENERAL ECONOMIC CONDITIONS AND CURRENCIES IN FOREIGN COUNTRIES;
- WEATHER CONDITIONS THAT VARY SIGNIFICANTLY FROM HISTORICALLY NORMAL CONDITIONS WHICH MAY ADVERSELY AFFECT THE DEMAND FOR PROPANE AND HERITAGE'S FINANCIAL CONDITION;
- HERITAGE'S SUCCESS IN HEDGING ITS PRODUCT SUPPLY POSITIONS;

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- THE EFFECTIVENESS OF RISK-MANAGEMENT POLICIES AND PROCEDURES AND THE ABILITY OF HERITAGE'S LIQUIDS MARKETING COUNTER PARTIES TO SATISFY THEIR FINANCIAL COMMITMENTS;
- THE GENERAL LEVEL OF PETROLEUM PRODUCT DEMAND AND THE AVAILABILITY AND PRICE OF PROPANE SUPPLIES;
- SUDDEN AND SHARP PROPANE PRICE INCREASES AND MARKET VOLATILITY MAY ADVERSELY AFFECT HERITAGE'S OPERATING RESULTS;
- THE POLITICAL AND ECONOMIC STABILITY OF PETROLEUM PRODUCING NATIONS;
- HERITAGE'S ABILITY TO CONDUCT BUSINESS IN FOREIGN COUNTRIES;
- HERITAGE'S ABILITY TO OBTAIN ADEQUATE SUPPLIES OF PROPANE FOR RETAIL SALE IN THE EVENT OF AN INTERRUPTION IN SUPPLY OR TRANSPORTATION;
- ENERGY PRICES GENERALLY AND SPECIFICALLY, THE PRICE OF PROPANE TO THE CONSUMER COMPARED TO THE PRICE OF ALTERNATIVE AND COMPETING FUELS;
- THE MATURITY OF THE PROPANE INDUSTRY AND COMPETITION FROM OTHER PROPANE DISTRIBUTORS AND OTHER ENERGY SOURCES;
- ENERGY EFFICIENCIES AND TECHNOLOGICAL TRENDS MAY AFFECT DEMAND FOR PROPANE;
- THE AVAILABILITY AND COST OF CAPITAL;
- HERITAGE'S ABILITY TO ACCESS CERTAIN CAPITAL SOURCES MAY REQUIRE IT TO OBTAIN A DEBT RATING;
- CHANGES IN LAWS AND REGULATIONS TO WHICH HERITAGE IS SUBJECT, INCLUDING TAX, ENVIRONMENTAL, TRANSPORTATION, AND EMPLOYMENT REGULATIONS;
- OPERATING RISKS INCIDENTAL TO TRANSPORTING, STORING, AND DISTRIBUTING PROPANE, INCLUDING LITIGATION RISKS WHICH MAY NOT BE COVERED BY INSURANCE;
- HERITAGE'S ABILITY TO GENERATE AVAILABLE CASH FOR DISTRIBUTIONS TO UNITHOLDERS;
- THE COSTS AND EFFECTS OF LEGAL AND ADMINISTRATIVE PROCEEDINGS AGAINST HERITAGE OR WHICH MAY BE BROUGHT AGAINST IT;
- HERITAGE'S ABILITY TO SUSTAIN HISTORICAL LEVELS OF INTERNAL GROWTH;
- HERITAGE'S ABILITY TO CONTINUE TO LOCATE AND ACQUIRE OTHER PROPANE COMPANIES AT PURCHASE PRICES THAT ARE ACCRETIVE TO ITS FINANCIAL RESULTS;

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- CASH DISTRIBUTIONS TO UNITHOLDERS ARE NOT GUARANTEED AND MAY FLUCTUATE WITH HERITAGE'S PERFORMANCE AND OTHER EXTERNAL FACTORS, INCLUDING RESTRICTIONS IN HERITAGE'S DEBT AGREEMENTS;

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AND

- HERITAGE MAY SELL ADDITIONAL LIMITED PARTNER INTERESTS, THUS DILUTING THE EXISTING INTEREST OF UNITHOLDERS.

### GENERAL

The retail propane business is a margin-based business in which gross profits depend on the excess of sales price over propane supply cost. The market price of propane is often subject to volatile changes as a result of supply or other market conditions over which Heritage will have no control. Product supply contracts are one-year agreements subject to annual renewal and generally permit suppliers to charge posted prices (plus transportation costs) at the time of delivery or the current prices established at major delivery points. Since rapid increases in the wholesale cost of propane may not be immediately passed on to retail customers, such increases could reduce gross profits. Heritage generally has attempted to reduce price risk by purchasing propane on a short-term basis. Heritage has on occasion purchased significant volumes of propane during periods of low demand, which generally occur during the summer months, at the then current market price, for storage both at its customer service locations and in major storage facilities for future resale.

The retail propane business of Heritage consists principally of transporting propane purchased in the contract and spot markets, primarily from major fuel suppliers, to its customer service locations and then to tanks located on the customers' premises, as well as to portable propane cylinders. In the residential and commercial markets, propane is primarily used for space heating, water heating, and cooking. In the agricultural market, propane is primarily used for crop drying, tobacco curing, poultry brooding, and weed control. In addition, propane is used for certain industrial applications, including use as an engine fuel that burns in internal combustion engines that power vehicles and forklifts and as a heating source in manufacturing and mining processes.

Since its formation in 1989, Heritage has grown primarily through acquisitions of retail propane operations and, to a lesser extent, through internal growth. Since its inception through August 31, 2002, Heritage completed 91 acquisitions for an aggregate purchase price approximating \$633 million, including the transfer by U.S. Propane of its propane operations to Heritage for \$181.4 million, plus working capital of approximately \$12.9 million. During the three months ended November 30, 2002, Heritage completed two acquisitions for an aggregate purchase price of \$2.5 million, which includes \$1.6 million in cash and \$0.9 million in notes payable on non-compete agreements and liabilities assumed. Subsequent to November 30, 2002, Heritage purchased the propane assets of V-1 Oil Co, which was one of the largest privately held propane marketers in the northwest. Management believes that Heritage is the fourth largest retail marketer of propane in the United States, based on retail gallons sold. Heritage now serves more than 650,000 customers from nearly 300 customer service locations in 29 states, following the acquisition of the propane assets of V-1.

Heritage's propane distribution business is largely seasonal and dependent upon weather conditions in its service areas. Propane sales to residential and commercial customers are affected by winter heating season requirements. Historically, approximately two-thirds of Heritage's retail propane volume and in excess of 80% of Heritage's EBITDA, as adjusted is attributable to sales during the six-month peak-heating season of October through March. This generally results in higher operating revenues and net income during the period from October through March of each year and lower operating revenues and either net losses or lower net income during the period from April through September of each year. Consequently, sales and operating profits are concentrated in the first and second fiscal quarters, however, cash flow from operations is generally greatest during the second and third fiscal quarters when customers pay for propane purchased during the six-month peak-heating season. Sales to

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industrial and agricultural customers are much less weather sensitive.

A substantial portion of Heritage's propane is used in the heating-sensitive residential and commercial markets causing the temperatures realized in Heritage's areas of operations, particularly during the six-month peak-heating season, to have a significant effect on its financial performance. In any given area, sustained warmer-than-normal temperatures will tend to result in reduced propane use, while sustained colder-than-normal temperatures will tend to result in greater propane use. Heritage uses information on normal temperatures in understanding how temperatures that are colder or warmer than normal affect historical results of operations and in preparing forecasts of future operations.

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Gross profit margins are not only affected by weather patterns, but also vary according to customer mix. For example, sales to residential customers generate higher margins than sales to certain other customer groups, such as commercial or agricultural customers. Wholesale margins are substantially lower than retail margins. In addition, gross profit margins vary by geographical region. Accordingly, a change in customer or geographic mix can affect gross profit without necessarily affecting total revenues.

Amounts discussed below reflect 100% of the results of MP Energy Partnership. MP Energy Partnership is a general partnership in which Heritage owns a 60% interest. Because MP Energy Partnership is primarily engaged in lower-margin wholesale distribution, its contribution to Heritage's net income is not significant and the minority interest of this partnership is excluded from the EBITDA, as adjusted calculation.

As stated above, during the fourth quarter of 2003, Heritage adopted the fair value recognition provisions of Statement of Financial Accounting Standards No. 123 Accounting for Stock-based Compensation (SFAS 123) effective as of September 1, 2002. Accordingly, the following information compares the originally reported consolidated statement of operations, reclassified for the adoption of EITF 02-3 for the three months ended November 30, 2002 and as adjusted for the adoption of SFAS 123:

	As Originally Reported	As adjusted for the adoption of SFAS 123
<b>REVENUES:</b>		
Retail fuel	\$ 84,050	\$ 84,050
Wholesale fuel	11,348	11,348
Liquids marketing, net	707	707
Other	17,355	17,355
	-----	-----
Total revenues	113,460	113,460
	-----	-----
<b>COSTS AND EXPENSES:</b>		
Cost of products sold	57,020	57,020
Operating expenses	33,425	33,392
Depreciation and amortization	9,266	9,266
Selling, general and administrative	3,192	2,856
	-----	-----
Total costs and expenses	102,903	102,534
	-----	-----
<b>OPERATING INCOME</b>	<b>10,557</b>	<b>10,926</b>

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OTHER INCOME (EXPENSE):		
Interest expense	(9,297)	(9,297)
Equity in earnings of affiliates	213	213
Gain on disposal of assets	67	67
Other	(278)	(278)
	-----	-----
INCOME (LOSS) BEFORE MINORITY INTERESTS	1,262	1,631
Minority interests	(123)	(127)
	-----	-----
NET INCOME (LOSS)	1,139	1,504
GENERAL PARTNER'S INTEREST IN NET INCOME (LOSS)	229	233
	-----	-----
LIMITED PARTNERS' INTEREST IN NET INCOME (LOSS)	\$ 910	\$ 1,271
	=====	=====
BASIC NET INCOME (LOSS) PER LIMITED PARTNER UNIT	\$ 0.06	\$ 0.08
	=====	=====
BASIC AVERAGE NUMBER OF UNITS OUTSTANDING	15,816,347	15,816,347
	=====	=====
DILUTED NET INCOME (LOSS) PER LIMITED PARTNER UNIT	\$ 0.06	\$ 0.08
	=====	=====
DILUTED AVERAGE NUMBER OF UNITS OUTSTANDING	15,848,698	15,848,698
	=====	=====

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THREE MONTHS ENDED NOVEMBER 30, 2002 COMPARED TO THE THREE MONTHS ENDED NOVEMBER 30, 2001

Volume. Total retail gallons sold in the three months ended November 30, 2002 were 76.7 million, an increase of 1.9 million over the 74.8 million gallons sold in the three months ended November 30, 2001. Of the 1.9 million gallon increase in volume, 1.6 million gallons reflects the benefits of the volume added through acquisitions and 0.3 million gallons from more favorable weather conditions in some of Heritage's areas of operations, offset by warmer than normal weather conditions in other areas of operations. Heritage also sold approximately 22.1 million wholesale gallons in this first quarter of fiscal 2003, a decrease of 1.2 million gallons from the 23.3 million wholesale gallons sold in the first quarter of fiscal 2002. U.S. wholesale gallons decreased 0.1 million gallons to 4.9 million gallons and the foreign volumes of MP Energy Partnership decreased 1.1 million gallons to 17.2 million for the first quarter.

Revenues. Total revenues for the three months ended November 30, 2002 were \$113.5 million, an increase of \$5.5 million, as compared to \$108.0 million in the three months ended November 30, 2001. The current period's domestic retail propane revenues increased \$0.8 million to \$84.0 million versus the prior year's revenues of \$83.2 million due to a \$0.3 million increase in retail volumes sold, a \$1.8 million increase due to acquisitions offset by \$1.3 million decrease due to slightly lower selling prices in the current period. The U.S. wholesale revenues decreased to \$2.5 million, as compared to \$3.1 million for the period ended November 30, 2001, primarily due to lower selling prices. Foreign revenues decreased \$0.6 million for the three months ended November 30, 2002 to \$8.9 million as compared to \$9.5 million for the three months ended November 30, 2001, as a result of decreased volumes described above. The net liquids marketing activity conducted through Resources was \$0.7 million versus the prior year's activity of \$(3.3) million due to more favorable movement in product prices in the current fiscal period. Other domestic revenues increased by \$1.9 million, to \$17.4 million as compared to \$15.5 million in the prior year as a result of acquisitions.

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Cost of Products Sold. Total cost of products sold decreased to \$57.0 million for the three months ended November 30, 2002 as compared to \$60.2 million for the three months ended November 30, 2001. The current period's domestic retail cost of sales decreased \$2.8 million to \$41.6 million as compared to \$44.4 million in the prior year of which, \$3.8 million was due to a lower cost of fuel per gallon this period offset by \$1.0 million increase due to slightly increased volumes compared to the same period last fiscal year. The U.S. wholesale cost of sales decreased to \$2.1 million as compared to \$2.9 million for the period ended November 30, 2001, of which \$0.7 million was due to lower wholesale fuel costs and \$0.1 million was due to slightly lower volumes than those incurred during the same period last fiscal year. Foreign cost of sales decreased \$0.8 million to \$8.4 million as compared to \$9.2 million in the prior year of which \$0.3 million was due to a decrease in wholesale fuel costs and \$0.5 million was due to lower volumes. Other cost of sales increased \$1.2 million to \$4.9 million as compared to \$3.7 million for the three months ended November 30, 2001.

Gross Profit. Total gross profit for the three months ended November 30, 2002 increased by \$8.7 million to \$56.4 million as compared to \$47.7 million for the three months ended November 30, 2001. For the three months ended November 30, 2002, retail fuel gross profit was \$42.4 million, U.S. wholesale was \$0.3 million, and other gross profit was \$12.5 million. Foreign wholesale gross profit was \$0.5 million and liquids marketing gross profit was \$0.7 million. As a comparison, for the three months ended November 30, 2001, Heritage recorded retail fuel gross profit of \$38.9 million, U.S. wholesale was \$0.2 million, and other gross profit was \$11.6 million. Foreign wholesale gross profit was \$0.3 million and liquids marketing was a loss of \$3.3 million for the three months ended November 30, 2001. The increase in gross profit is primarily attributable to lower fuel costs and slightly increased volumes, offset by slightly lower selling prices.

Operating Expenses. Operating expenses were \$33.4 million for the three months ended November 30, 2002 as compared to \$31.8 million for the three months ended November 30, 2001. The increase of \$1.6 million is primarily the result of a \$0.7 million increase in employee-related costs, and a \$0.7 million increase related to industry-wide increases in business insurance costs.

Selling, General and Administrative. Selling, general and administrative expenses were \$2.8 million for the three months ended November 30, 2002, a \$0.1 million decrease from the \$2.9 million for the same three-month period last year. Of the decrease, \$0.2 million was related to the adoption of SFAS 123 described above.

Depreciation and Amortization. Depreciation and amortization was \$9.3 million in the three months ended November 30, 2002 as compared to \$9.1 million in the three months ended November 30, 2001. This increase is

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due to additional depreciation and amortization of property, plant and equipment, and other intangible assets from acquisitions.

Operating Income. For the three months ended November 30, 2002, Heritage had operating income of \$10.9 million as compared to operating income of \$3.9 million for the three months ended November 30, 2001. This increase is a combination of an increase of \$0.2 million related to the adoption of SFAS 123, and increased gross profit offset by increased operating expenses described above.

Interest Expense. Interest expense increased \$0.1 million for the three

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months ended November 30, 2002 to \$9.3 million from \$9.2 million for the same three-month period last year.

Net Income(Loss). For the three month period ended November 30, 2002, Heritage had net income of \$1.5 million, an increase of \$6.3 million as compared to a net loss for the three months ended November 30, 2001 of \$4.8 million. The increase is primarily the result of an increase of \$0.2 million relating to the adoption of SFAS 123 and the increase in operating income related to operating performance described above.

EBITDA, as adjusted. EBITDA, as adjusted increased \$7.1 million to \$20.8 million for the three months ended November 30, 2002, as compared to EBITDA, as adjusted of \$13.7 million for the period ended November 30, 2001. This increase is due to the operating conditions described above, and is a record level EBITDA, as adjusted for the first quarter results of Heritage. EBITDA, as adjusted for the three months ended November 30, 2002 and November 30, 2001 is computed as follows:

NET INCOME RECONCILIATION ----- (in millions)	Three Months Ended November 30, -----	
	2002	2001
	-----	-----
Net income (loss)	\$ 1.5	\$ (4.8)
Depreciation and amortization	9.3	9.1
Interest	9.3	9.2
Non-cash compensation expense	0.3	0.5
Other expense	0.3	0.1
Depreciation, amortization, and interest of investee	0.2	0.1
Minority interest in the Operating Partnership	-	(0.1)
Less: Gain on disposal of assets	(0.1)	(0.4)
	-----	-----
EBITDA, as adjusted (a)	\$ 20.8	\$ 13.7
	-----	-----

- (a) EBITDA, as adjusted is defined as the Partnership's earnings before interest, taxes, depreciation, amortization and other non-cash items, such as compensation charges for unit issuances to employees, gain or loss on disposal of assets, and other expenses. We present EBITDA, as adjusted, on a Partnership basis which includes both the general and limited partner interests. Non-cash compensation expense represents charges for the value of the Common Units awarded under the Partnership's compensation plans that have not yet vested under the terms of those plans and are charges which do not, or will not, require cash settlement. Non-cash income such as the gain arising from our disposal of assets is not included when determining EBITDA, as adjusted. EBITDA, as adjusted (i) is not a measure of performance calculated in accordance with generally accepted accounting principles and (ii) should not be considered

in isolation or as a substitute for net income, income from operations or cash flow as reflected in our consolidated financial statements.

EBITDA, as adjusted is presented because such information is relevant and is used by management, industry analysts, investors, lenders and

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rating agencies to assess the financial performance and operating results of the Partnership's fundamental business activities. Management believes that the presentation of EBITDA, as adjusted is useful to lenders and investors because of its use in the propane industry and for master limited partnerships as an indicator of the strength and performance of the Partnership's ongoing business operations, including the ability to fund capital expenditures, service debt and pay distributions. Additionally, management believes that EBITDA, as adjusted provides additional and useful information to the Partnership's investors for trending, analyzing and benchmarking the operating results of the Partnership from period to period as compared to other companies that may have different financing and capital structures. The presentation of EBITDA, as adjusted allows investors to view the Partnership's performance in a manner similar to the methods used by management and provides additional insight to the Partnership's operating results.

EBITDA, as adjusted is used by management to determine our operating performance, and along with other data as internal measures for setting annual operating budgets, assessing financial performance of the Partnership's numerous business locations, as a measure for evaluating targeted businesses for acquisition and as a measurement component of incentive compensation. The Partnership has a large number of business locations located in different regions of the United States. EBITDA, as adjusted can be a meaningful measure of financial performance because it excludes factors which are outside the control of the employees responsible for operating and managing the business locations, and provides information management can use to evaluate the performance of the business locations, or the region where they are located, and the employees responsible for operating them. To present EBITDA, as adjusted on a full Partnership basis, we add back the minority interest of the general partner because net income is reported net of the general partner's minority interest. Our EBITDA, as adjusted includes non-cash compensation expense which is a non-cash expense item resulting from our unit based compensation plans that does not require cash settlement and is not considered during management's assessment of the operating results of the Partnership's business. By adding these non-cash compensation expenses in EBITDA, as adjusted allows management to compare the Partnership's operating results to those of other companies in the same industry who may have compensation plans with levels and values of annual grants that are different than the Partnership's. Other expenses include other finance charges and other asset non-cash impairment charges that are reflected in the Partnership's operating results but are not classified in interest, depreciation and amortization. We do not include gain on the sale of assets when determining EBITDA, as adjusted since including non-cash income resulting from the sale of assets increases the performance measure in a manner that is not related to the true operating results of the Partnership's business. In addition, Heritage's debt agreements contain financial covenants based on EBITDA, as adjusted. For a description of these covenants, please read "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations-Description of Indebtedness" included in the Partnership's Form 10-K/A for the fiscal year ended August 31, 2002, as filed with the Securities and Exchange Commission on November 26, 2003.

There are material limitations to using a measure such as EBITDA, as adjusted, including the difficulty associated with using it as the sole measure to compare the results of one company to another, and the inability to analyze certain significant items that directly affect a company's net income or loss. In addition, Heritage's calculation of EBITDA, as adjusted may not be consistent with similarly titled

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measures of other companies and should be viewed in conjunction with measurements that are computed in accordance with GAAP. EBITDA, as adjusted for the periods described herein is calculated in the same manner as presented by Heritage in the past. Management compensates for these limitations by considering EBITDA, as adjusted in conjunction with its analysis of other GAAP financial measures, such as gross profit, net income (loss), and cash flow from operating activities.

We have provided a reconciliation of EBITDA, as adjusted to net income(loss).

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### LIQUIDITY AND CAPITAL RESOURCES

The ability of Heritage to satisfy its obligations will depend on its future performance, which will be subject to prevailing economic, financial, business and weather conditions, and other factors, many of which are beyond management's control. Future capital requirements of Heritage are expected to be provided by cash flows from operating activities. To the extent future capital requirements exceed cash flows from operating activities:

- a) working capital will be financed by the working capital line of credit and repaid from subsequent seasonal reductions in inventory and accounts receivable;
- b) growth capital expenditures, mainly for customer tanks, will be financed by the revolving acquisition bank line of credit; and
- c) acquisition capital expenditures will be financed by the revolving acquisition bank line of credit; other lines of credit, long term debt, issuance of additional Common Units or a combination thereof.

Operating Activities. Cash used in operating activities during the three months ended November 30, 2002, was \$2.3 million as compared to cash provided by operating activities of \$0.1 million for the same three-month period ended November 30, 2001. The net cash used in operations for the three months ended November 30, 2002 consisted of net income of \$1.5 million and non-cash charges of \$9.5 million, principally depreciation and amortization, offset by the impact of an increase in working capital of \$13.3 million. The increase in working capital for the quarter ended November 30, 2002 as compared to the quarter ended November 30, 2001 is primarily due to the effect of timing of collection of the high accounts receivable related to the cold winter of fiscal 2001 and the timing of the purchase of inventory between the two periods.

Investing Activities. Heritage completed two acquisitions during the three months ended November 30, 2002 spending a net of \$1.6 million, after deducting cash received in such acquisitions. This capital expenditure amount is reflected in the cash used in investing activities of \$9.8 million along with \$9.7 million invested for maintenance needed to sustain operations at current levels and for customer tanks to support growth of operations. Cash used in investing activities also includes proceeds from the sale of idle property of \$1.5 million.

Financing Activities. Cash provided by financing activities during the three months ended November 30, 2002 of \$12.7 million resulted mainly from a net increase in the Working Capital Facility of \$22.6 million and a net increase in the Acquisition Facility of \$1.3 million used to acquire other propane businesses. These increases were offset by cash distributions to Unitholders of \$10.4 million and payments on other long-term debt of \$0.8 million.

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### FINANCING AND SOURCES OF LIQUIDITY

Heritage has a Bank Credit Facility with various financial institutions, which includes a Working Capital Facility, providing for up to \$65.0 million of borrowings for working capital and other general partnership purposes, and an Acquisition Facility providing for up to \$50.0 million of borrowings for acquisitions and improvements. The weighted average interest rate was 3.255% for the amounts outstanding at November 30, 2002 on both the Working Capital Facility and the Acquisition Facility. As of November 30, 2002, the Working Capital Facility had \$12.2 million available for borrowings and the Acquisition Facility had \$34.7 million available to fund future acquisitions. Subsequent to November 30, 2002, approximately \$17.3 million was drawn on the Acquisition Facility to fund the acquisition of V-1. Management believes that its Bank Credit Facility is adequate to fund the future operating and capital needs of the Partnership.

Heritage uses its cash provided by operating and financing activities to provide distributions to the Partnership's Unitholders and to fund acquisition, maintenance, and growth capital expenditures. Acquisition capital expenditures, which include expenditures related to the acquisition of retail propane operations and intangibles associated with such acquired businesses, were \$1.6 million for the three months ended November 30, 2002. In addition to the \$1.6 million of cash expended for acquisitions, \$0.5 million for notes payable on non-compete agreements were issued and liabilities of \$0.4 million were assumed in connection with certain acquisitions.

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Under the Partnership Agreement, the Partnership will distribute to its partners within 45 days after the end of each fiscal quarter, an amount equal to all of its Available Cash for such quarter. Available cash generally means, with respect to any quarter of the Partnership, all cash on hand at the end of such quarter less the amount of cash reserves established by the General Partner in its reasonable discretion that is necessary or appropriate to provide for future cash requirements. The Partnership's commitment to its Unitholders is to distribute the increase in its cash flow while maintaining prudent reserves for the Partnership's operations. The Partnership paid a quarterly distribution of \$0.6375 (or \$2.55 annually) on October 15, 2002 for the fourth quarter ended August 31, 2002, and declared a distribution of \$0.6375 (or \$2.55 annually) on December 18, 2002 payable on January 14, 2003. The current distribution level includes incentive distributions payable to the General Partner to the extent the quarterly distribution exceeds \$0.55 per unit (\$2.20 annually).

The assets utilized in the propane business do not typically require lengthy manufacturing process time or complicated, high technology components. Accordingly, the Partnership does not have any significant financial commitments for capital expenditures. In addition, the Partnership has not experienced any significant increases attributable to inflation in the cost of these assets or in its operations.

### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

Heritage has little cash flow exposure due to rate changes for long-term debt obligations. The Operating Partnership had \$68.1 million of variable rate debt outstanding as of November 30, 2002 through its Bank Credit Facility described elsewhere in this report. The balance outstanding in the Bank Credit Facility generally fluctuates throughout the year. A theoretical change of 1% in the interest rate on the balance outstanding at November 30, 2002 would result in an approximate \$681 thousand change in annual net income. Heritage primarily enters debt obligations to support general corporate purposes including capital

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expenditures and working capital needs. The Operating Partnership's long-term debt instruments were typically issued at fixed interest rates. When these debt obligations mature, Heritage may refinance all or a portion of such debt at then-existing market interest rates which may be more or less than the interest rates on the maturing debt.

Commodity price risk arises from the risk of price changes in the propane inventory that Heritage buys and sells. The market price of propane is often subject to volatile changes as a result of market conditions over which management will have no control. In the past, price changes have generally been passed along to Heritage's customers to maintain gross margins, mitigating the commodity price risk. In order to help ensure that adequate supply sources are available to Heritage during periods of high demand, Heritage will, from time to time, purchase significant volumes of propane during periods of low demand, which generally occur during the summer months, at the then current market price, for storage both at its customer service centers and in major storage facilities and for future delivery.

Heritage also attempts to minimize the effects of market price fluctuations for its propane supply by entering into certain financial contracts. In order to manage a portion of its propane price market risk, Heritage uses contracts for the forward purchase of propane, propane fixed-price supply agreements, and derivative commodity instruments such as price swap and option contracts. Swap instruments are a contractual agreement to exchange obligations of money between the buyer and seller of the instruments as propane volumes during the pricing period are purchased. Swaps are tied to a fixed price bid by the buyer and a floating price determination for the seller based on certain indices at the end of the relevant trading period. Heritage has entered into these swap instruments in the past to hedge the projected propane volumes to be purchased during each of the one-month periods during the projected heating season.

At November 30, 2002, Heritage had no outstanding propane hedges. Heritage continues to monitor propane prices and may enter into additional propane hedges in the future. Inherent in the portfolio from the liquids marketing activities are certain business risks, including market risk and credit risk. Market risk is the risk that the value of the portfolio will change, either favorably or unfavorably, in response to changing market conditions. Credit risk is the risk of loss from nonperformance by suppliers, customers, or financial counter parties to a contract. Heritage takes an active role in managing and controlling market and credit risk and has established control procedures which are reviewed on an ongoing basis. Heritage monitors market risk through a variety of techniques, including routine reporting to senior management. Heritage attempts to minimize credit risk exposure through credit policies and periodic monitoring procedures.

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### LIQUIDS MARKETING

Heritage buys and sells derivative financial instruments, which are within the scope of SFAS 133 and that are not designated as accounting hedges. Heritage also enters into energy trading contracts, which are not derivatives, and therefore are not within the scope of SFAS 133. EITF Issue No. 98-10, Accounting for Contracts Involved in Energy Trading and Risk Management Activities (EITF 98-10), applied to energy trading contracts not within the scope of SFAS 133 that were entered into prior to October 25, 2002. The types of contracts Heritage utilizes in its liquids marketing segment include energy commodity forward contracts, options, and swaps traded on the over-the-counter financial markets. In accordance with the provisions of SFAS 133, derivative financial instruments utilized in connection with Heritages' liquids marketing activity are accounted for using the mark-to-market method. Additionally, all energy

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trading contracts entered into prior to October 25, 2002 were accounted for using the mark-to-market method in accordance with the provisions of EITF 98-10. Under the mark-to-market method of accounting, forwards, swaps, options, and storage contracts are reflected at fair value, and are shown in the consolidated balance sheet as assets and liabilities from liquids marketing activities. As of August 31, 2002, Heritage adopted the applicable provisions of EITF Issue No. 02-3, Issues Related to Accounting for Contracts Involved in Energy Trading and Risk Management Activities (EITF 02-3), which requires that gains and losses on derivative instruments be shown net in the statement of operations if the derivative instruments are held for trading purposes. Net realized and unrealized gains and losses from the financial contracts and the impact of price movements are recognized in the statement of operations as liquids marketing revenue. Changes in the assets and liabilities from the liquids marketing activities result primarily from changes in the market prices, newly originated transactions, and the timing and settlement of contracts. EITF 02-3 also rescinds EITF 98-10 for all energy trading contracts entered into after October 25, 2002 and specifies certain disclosure requirements. Consequently, Heritage does not apply mark-to-market accounting for any contracts entered into after October 25, 2002 that are not within the scope of SFAS 133. Heritage attempts to balance its contractual portfolio in terms of notional amounts and timing of performance and delivery obligations. However, net unbalanced positions can exist or are established based on management's assessment of anticipated market movements.

The adoption of EITF 02-3 requires that realized and unrealized gains and losses be shown net for all periods presented. The following table summarizes the amounts that have been reclassified in the statement of operations:

	For the Three Months Ended November 30,	
	2002	2001
	-----	-----
Revenue - liquids marketing	\$ 60,730	\$ 50,820
Costs and expenses - liquids marketing	(60,023)	(54,145)
	-----	-----
Net, as reclassified	\$ 707	\$ (3,325)
	=====	=====

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The notional amounts and terms of these financial instruments as of November 30, 2002 and 2001 include fixed price payor for 586,000 and 1,592,500 barrels of propane and butane, and fixed price receiver of 440,000 and 1,221,964 barrels of propane and butane, respectively. Notional amounts reflect the volume of the transactions, but do not represent the amounts exchanged by the parties to the financial instruments. Accordingly, notional amounts do not accurately measure Heritage's exposure to market or credit risks.

The fair value of the financial instruments related to liquids marketing activities as of November 30, 2002 and August 31, 2002, was assets of \$0.8 and \$2.3 million respectively, and liabilities of \$0.8 and \$1.8 million, respectively, related to propane and butane.

Estimates related to Heritage's liquids marketing activities are sensitive to uncertainty and volatility inherent in the energy commodities markets and actual results could differ from these estimates. A theoretical change of 10% in the underlying commodity value of the liquids marketing contracts would result in an

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approximate \$273 change in the market value of the contracts as there were approximately 6.1 million gallons of net unbalanced positions at November 30, 2002.

Inherent in the resulting contractual portfolio are certain business risks, including market risk and credit risk. Market risk is the risk that the value of the portfolio will change, either favorably or unfavorably, in response to changing market conditions. Credit risk is the risk of loss from nonperformance by suppliers, customers, or financial counterparties to a contract. Heritage takes an active role in managing and controlling market and credit risk and have established control procedures, which are reviewed on an ongoing basis. Heritage monitors market risk through a variety of techniques, including routine reporting to senior management. Heritage attempts to minimize credit risk exposure through credit policies and periodic monitoring procedures.

The following table summarizes the fair value of Heritage's contracts, aggregated by method of estimating fair value of the contracts as of November 30, 2002 and August 31, 2002 where settlement had not yet occurred. Heritage's contracts all have a maturity of less than 1 year. The market prices used to value these transactions reflect management's best estimate considering various factors including closing average spot prices for the current and outer months plus a differential to consider time value and storage costs.

Source of Fair Value	November 30, 2002	August 31, 2002
-----	-----	-----
Prices actively quoted	\$ 616	\$ 1,276
Prices based on other valuation methods	197	1,025
	-----	-----
Assets from liquids marketing	\$ 813	\$ 2,301
	=====	=====
Prices actively quoted	\$ 585	\$ 669
Prices based on other valuation methods	187	1,149
	-----	-----
Liabilities from liquids marketing	\$ 772	\$ 1,818
	=====	=====
Unrealized gains in fair value of contracts outstanding	\$ 41	\$ 483
	=====	=====

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The following table summarizes the changes in the unrealized fair value of Heritage's contracts where settlement had not yet occurred for the three months ending November 30, 2002 and 2001.

	November 30, 2002	November 30, 2001
	-----	-----
Unrealized gains (losses) in fair value of contracts outstanding at the beginning of the period	\$ 483	\$ (665)
Other unrealized gains (losses) recognized during the period	224	(2,660)
Less: Realized gains (losses) recognized during the period	666	(801)

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	-----	-----
Unrealized gains (losses) in fair value of contracts outstanding at the end of the period	\$ 41	\$ (2,524)
	=====	=====

The following table summarizes the gross transaction volumes in barrels for liquids marketing contracts that were physically settled for the three months ended November 30, 2002, and 2001.

(in thousands)

Three months ended November 30, 2002	44
Three months ended November 30, 2001	112

### ITEM 4. CONTROLS AND PROCEDURES

The Partnership maintains controls and procedures designed to ensure that information required to be disclosed in the reports that the Partnership files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the SEC. Within 90 days prior to the filing date of this report, an evaluation was performed under the supervision and with the participation of the Partnership's management, including the Chief Executive Officer and the Chief Financial Officer of the General Partner of the Partnership, of the effectiveness of the design and operation of the Partnership's disclosure controls and procedures (as such terms are defined in Rule 13a-14(c) and 15d-14(c) of the Exchange Act). Based upon that evaluation, management, including the Chief Executive Officer and the Chief Financial Officer of the General Partner of the Partnership, concluded that the Partnership's disclosure controls and procedures were adequate and effective as of November 30, 2002. There have been no significant changes in the Partnership's internal controls or in other factors subsequent to such evaluation, and there have been no corrective actions with respect to significant deficiencies and material weaknesses in our internal controls.

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## PART II - OTHER INFORMATION

### ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

#### (a) Exhibits

The exhibits listed on the following Exhibit Index are filed as part of this Report. Exhibits required by Item 601 of Regulation S-K, but which are not listed below, are not applicable.

	Exhibit Number	Description
	-----	-----
(1)	3.1	Agreement of Limited Partnership of Heritage Propane Partners, L.P.
(10)	3.1.1	Amendment No. 1 to Amended and Restated Agreement of Limited Partnership of Heritage Propane Partners, L.P.

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- (16) 3.1.2 Amendment No. 2 to Amended and Restated Agreement of Limited Partnership of Heritage Propane Partners, L.P.
- (19) 3.1.3 Amendment No. 3 to Amended and Restated Agreement of Limited Partnership of Heritage Propane Partners, L.P.
- (19) 3.1.4 Amendment No. 4 to Amended and Restated Agreement of Limited Partnership of Heritage Propane Partners, L.P.
- (1) 3.2 Agreement of Limited Partnership of Heritage Operating, L.P.
- (12) 3.2.1 Amendment No. 1 to Amended and Restated Agreement of Limited Partnership of Heritage Operating, L.P.
- (19) 3.2.2 Amendment No. 2 to Amended and Restated Agreement of Limited Partnership of Heritage Operating, L.P.
- (18) 3.3 Amended Certificate of Limited Partnership of Heritage Propane Partners, L.P.
- (18) 3.4 Amended Certificate of Limited Partnership of Heritage Operating, L.P.
- (20) 4.1 Registration Rights Agreement for Limited Partner Interests of Heritage Propane Partners, L.P.
- (7) 10.1 First Amended and Restated Credit Agreement with Banks Dated May 31, 1999
- (8) 10.1.1 First Amendment to the First Amended and Restated Credit Agreement dated as of May 15, 1999
- (9) 10.1.2 Second Amendment to First Amended and Restated Credit Agreement dated as of May 15, 1999
- (10) 10.1.3 Third Amendment dated as of August 10, 2000 to First Amended and Restated Credit Agreement
- (13) 10.1.4 Fourth Amendment to First Amended and Restated Credit Agreement dated as of December 15, 2000

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Exhibit Number	Description
(16)	10.1.5 Fifth Amendment to First Amended and Restated Credit Agreement dated as of July 15, 1999
(1)	10.2 Form of Note Purchase Agreement (June 25, 1996)
(3)	10.2.1 Amendment of Note Purchase Agreement (June 25, 1996) dated as of July 25, 1996
(4)	10.2.2 Amendment of Note Purchase Agreement (June 25, 1996) dated as of March 11, 1999
(6)	10.2.3 Amendment of Note Purchase Agreement (June 25, 1996) dated as of October 15, 1999
(8)	10.2.4 Second Amendment Agreement dated September 1, 1999 to June 25, 1996 Note Purchase Agreement
(11)	10.2.5 Third Amendment Agreement dated May 31, 2000 to June 25, 1996 Note Purchase Agreement

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November 19, 1997 Note Purchase Agreement

- (10) 10.2.6 Fourth Amendment Agreement dated August 10, 2000 to June 25, 1996 Note Purchase Agreement and November 19, 1997 Note Purchase Agreement
- (13) 10.2.7 Fifth Amendment Agreement dated as of December 28, 2000 to June 25, 1996 Note Purchase Agreement, November 19, 1997 Note Purchase Agreement and August 10, 2000 Note Purchase Agreement
- (1) 10.3 Form of Contribution, Conveyance and Assumption Agreement among Heritage Holders, Heritage Propane Partners, L.P. and Heritage Operating, L.P.
- (1) 10.6 Restricted Unit Plan
- (4) 10.6.1 Amendment of Restricted Unit Plan dated as of October 17, 1996
- (12) 10.6.2 Amended and Restated Restricted Unit Plan dated as of August 10, 2000
- (18) 10.6.3 Second Amended and Restated Restricted Unit Plan dated as of February 4, 2002
- (12) 10.7 Employment Agreement for James E. Bertelsmeyer dated as of August 10, 2000
- (18) 10.7.1 Consent to Assignment of Employment Agreement for James E. Bertelsmeyer dated February 3, 2002
- (21) 10.7.2 Amendment 1 of Employment Agreement for James E. Bertelsmeyer dated August 10, 2000
- (12) 10.8 Employment Agreement for R. C. Mills dated as of August 10, 2000
- (18) 10.8.1 Consent to Assignment of Employment Agreement for R.C. Mills dated February 3, 2002
- (12) 10.9 Employment Agreement for Larry J. Dagley dated as of August 10, 2000
- (18) 10.9.1 Consent to Assignment of Employment Agreement for Larry J. Dagley dated February 3, 2002
- (12) 10.10 Employment Agreement for H. Michael Krimbill dated as of August 10, 2000

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Exhibit Number	Description
(18) 10.10.1	Consent to Assignment of Employment Agreement for H. Michael Krimbill dated February 3, 2002
(12) 10.11	Employment Agreement for Bradley K. Atkinson dated as of August 10, 2000
(18) 10.11.1	Consent to Assignment of Employment Agreement for Bradley K. Atkinson dated February 3, 2002
(7) 10.12	First Amended and Restated Revolving Credit Agreement between Heritage Service Corp. and Banks Dated May 31, 1999
(16) 10.12.1	First Amendment to First Amended and Restated Revolving Credit Agreement, dated May 15, 1999
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- 10, 2000
- (16) 10.12.3 Third Amendment to First Amended and Restated Revolving Credit Agreement, dated 28, 2000
  - (16) 10.12.4 Fourth Amendment to First Amended and Restated Revolving Credit Agreement, dated 2001
  - (12) 10.13 Employment Agreement for Mark A. Darr dated as of August 10, 2000
  - (18) 10.13.1 Consent to Assignment of Employment Agreement for Mark A. Darr dated February
  - (12) 10.14 Employment Agreement for Thomas H. Rose dated as of August 10, 2000
  - (18) 10.14.1 Consent to Assignment of Employment Agreement for Thomas H. Rose dated February
  - (12) 10.15 Employment Agreement for Curtis L. Weishahn dated as of August 10, 2000
  - (18) 10.15.1 Consent to Assignment of Employment Agreement for Curtis L. Weishahn dated February 2002
  - (5) 10.16 Note Purchase Agreement dated as of November 19, 1997
  - (6) 10.16.1 Amendment dated October 15, 1998 to November 19, 1997 Note Purchase Agreement
  - (8) 10.16.2 Second Amendment Agreement dated September 1, 1999 to November 19, 1997 Note Purchase Agreement and June 25, 1996 Note Purchase Agreement
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  - (13) 10.16.5 Fifth Amendment Agreement dated as of December 28, 2000 to June 25, 1996 Note Purchase Agreement, November 19, 1997 Note Purchase Agreement and August 10, 2000 Note Purchase Agreement

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Exhibit Number	Description
(10) 10.17	Contribution Agreement dated June 15, 2000 among U.S. Propane, L.P., Heritage L.P. and Heritage Propane Partners, L.P.
(10) 10.17.1	Amendment dated August 10, 2000 to June 15, 2000 Contribution Agreement
(10) 10.18	Subscription Agreement dated June 15, 2000 between Heritage Propane Partners, individual investors
(10) 10.18.1	Amendment dated August 10, 2000 to June 15, 2000 Subscription Agreement
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- (10) 10.19 Note Purchase Agreement dated as of August 10, 2000
- (13) 10.19.1 Fifth Amendment Agreement dated as of December 28, 2000 to June 25, 1996 Note Agreement, November 19, 1997 Note Purchase Agreement and August 10, 2000 Note Agreement
- (14) 10.19.2 First Supplemental Note Purchase Agreement dated as of May 24, 2001 to the August 10, 2000 Note Purchase Agreement
- (15) 10.20 Stock Purchase Agreement dated as of July 5, 2001 among the shareholders of Propane Inc. and Heritage Holdings, Inc.
- (15) 10.21 Stock Purchase Agreement dated as of July 5, 2001 among the shareholders of California Western Gas, Inc. and Heritage Holdings, Inc.
- (15) 10.22 Agreement and Plan of Merger dated as of July 5, 2001 among California Western Gas Company, the Majority Stockholders of California Western Gas Company signatories thereto, Heritage Holdings, Inc. and California Western Merger Corp.
- (15) 10.23 Agreement and Plan of Merger dated as of July 5, 2001 among Growth Properties, Inc., the Majority Shareholders signatories thereto, Heritage Holdings, Inc. and Growth Properties Merger Corp.
- (15) 10.24 Asset Purchase Agreement dated as of July 5, 2001 among L.P.G. Associates, the Shareholders of L.P.G. Associates and Heritage Operating, L.P.
- (15) 10.25 Asset Purchase Agreement dated as of July 5, 2001 among WMJB, Inc., the Shareholders of WMJB, Inc. and Heritage Operating, L.P.
- (15) 10.25.1 Amendment to Asset Purchase Agreement dated as of July 5, 2001 among WMJB, Inc., the Shareholders of WMJB, Inc. and Heritage Operating, L.P.
- (18) 10.26 Assignment, Conveyance and Assumption Agreement between U.S. Propane, L.P. and Heritage Holdings, Inc., as the former General Partner of Heritage Propane Partners, L.P., dated February 4, 2002
- (18) 10.27 Assignment, Conveyance and Assumption Agreement between U.S. Propane, L.P. and Heritage Holdings, Inc., as the former General Partner of Heritage Operating, L.P., dated February 4, 2002

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Exhibit Number	Description
(22) 10.28	Assignment for Contribution of Assets in Exchange for Partnership Interest dated February 9, 2002 amount V-1 Oil Co., the shareholders of V-1 Oil Co., Heritage Propane Partners, L.P. and Heritage Operating, L.P.
(**) 10.29	Employment Agreement for Michael L. Greenwood dated as of July 1, 2002
(21) 21.1	List of Subsidiaries
(*) 31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

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- (\*) 31.2 Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- (\*) 32.1 Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, a pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- (\*) 32.2 Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, a pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

-----

- (1) Incorporated by reference to the same numbered Exhibit to Registrant's Registration Statement of Form S-1, File No. 333-04018, filed with the Commission on June 21, 1996.
- (2) Incorporated by reference to Exhibit 10.11 to Registrant's Registration Statement on Form S-1, File No. 333-04018, filed with the Commission on June 21, 1996.
- (3) Incorporated by reference to the same numbered Exhibit to Registrant's Form 10-Q for the quarter ended November 30, 1996.
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- (9) Incorporated by reference to the same numbered Exhibit to the Registrant's Form 10-Q for the quarter ended May 31, 2000.
- (10) Incorporated by reference to the same numbered Exhibit to the Registrant's Form 8-K dated August 23, 2000.

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- (11) File as Exhibit 10.16.3.
- (12) Incorporated by reference to the same numbered Exhibit to the Registrant's Form 10-K for the year ended August 31, 2000.
- (13) Incorporated by reference to the same numbered Exhibit to the Registrant's Form 10-Q for the quarter ended February 28, 2001.
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- (20) Incorporated by reference to the same numbered Exhibit to the Registrant's Form 8-K dated February 4, 2002.
- (21) Incorporated by reference to the same numbered Exhibit to the Registrant's Form 10-K for the year ended August 31, 2002.
- (22) Incorporated by reference to the same numbered Exhibit to the Registrant's Form 8-K dated January 6, 2003.
- (\*) Filed herewith.
- (\*\*) Filed with the January 14, 2003 Original Filing.
- (b) Reports on Form 8-K

The Partnership filed no reports on Form 8-K during the three months ended November 30, 2002.

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SIGNATURE

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

HERITAGE PROPANE PARTNERS, L.P.

By: U.S. Propane, L.P., General Partner

By: U.S. Propane, L.L.C., General Partner

Date: November 26, 2003

By: /s/ Michael L. Greenwood

-----  
Michael L. Greenwood

(Vice President, Chief

Financial Officer and officer duly authorized to sign on behalf of the registrant)

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INDEX TO EXHIBITS

Exhibit Number	Description
(1) 3.1	Agreement of Limited Partnership of Heritage Propane Partners, L.P.

## Edgar Filing: HERITAGE PROPANE PARTNERS L P - Form 10-Q/A

(10)	3.1.1	Amendment No. 1 to Amended and Restated Agreement of Limited Partnership of Heritage Propane Partners, L.P.
(16)	3.1.2	Amendment No. 2 to Amended and Restated Agreement of Limited Partnership of Heritage Propane Partners, L.P.
(19)	3.1.3	Amendment No. 3 to Amended and Restated Agreement of Limited Partnership of Heritage Propane Partners, L.P.
(19)	3.1.4	Amendment No. 4 to Amended and Restated Agreement of Limited Partnership of Heritage Propane Partners, L.P.
(1)	3.2	Agreement of Limited Partnership of Heritage Operating, L.P.
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(15) 10.21	Stock Purchase Agreement dated as of July 5, 2001 among the shareholders of Coast Liquid Gas, Inc. and Heritage Holdings, Inc.
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## Edgar Filing: HERITAGE PROPANE PARTNERS L P - Form 10-Q/A

(15)	10.24	Asset Purchase Agreement dated as of July 5, 2001 among L.P.G. Associates, the Shareholders of L.P.G. Associates and Heritage Operating, L.P.
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- (4) Incorporated by reference to the same numbered Exhibit to Registrant's Form 10-Q for the quarter ended February 28, 1997.
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