NuStar Energy L.P.
Form 10-Q
November 06, 2014

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2014

OR

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

For the transition period from _______ to _______

Commission File Number 1-16417

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

Delaware	74-2956831
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
19003 IH-10 West San Antonio, Texas	78257
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code (210) 918-2000

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule12b-2 of the Exchange Act:

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

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

The number of common units outstanding as of October 31, 2014 was 77,886,078.

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PART I – FINANCIAL INFORMATION

Item 1. Financial Statements
NUSTAR ENERGY L.P. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(Thousands of Dollars, Except Unit Data)

	September 30, 2014 (Unaudited)	December 31, 2013
Assets		
Current assets:		
Cash and cash equivalents	$25,686	$100,743
Accounts receivable, net of allowance for doubtful accounts of $306 and $1,224 as of September 30, 2014 and December 31, 2013, respectively	220,841	281,310
Receivable from related parties	45	51,084
Inventories	117,937	138,147
Income tax receivable	3,661	826
Other current assets	37,523	39,452
Assets held for sale	2,256	21,987
Total current assets	407,949	633,549
Property, plant and equipment, at cost	4,706,896	4,500,837
Accumulated depreciation and amortization	(1,315,466)	(1,190,184)
Property, plant and equipment, net	3,391,430	3,310,653
Intangible assets, net	61,815	71,249
Goodwill	617,429	617,429
Investment in joint ventures	72,872	68,735
Deferred income tax asset	4,902	5,769
Note receivable from related party	—	165,440
Other long-term assets, net	320,970	159,362
Total assets	$4,877,367	$5,032,186
Liabilities and Partners' Equity		
Current liabilities:		
Accounts payable	$177,961	$298,751
Payable to related party	14,119	8,325
Short-term debt	21,400	—
Accrued interest payable	27,501	33,113
Accrued liabilities	39,053	38,632
Taxes other than income tax	15,053	9,745
Income tax payable	4,035	4,006
Total current liabilities	299,122	392,572
Long-term debt	2,731,551	2,655,553
Long-term payable to related party	30,489	41,139
Deferred income tax liability	27,785	27,350
Other long-term liabilities	19,775	11,778
Commitments and contingencies (Note 5)		
Partners' equity:		
Limited partners (77,886,078 common units outstanding as of September 30, 2014 and December 31, 2013)	1,788,360	1,921,726

General partner	40,419	43,804
Accumulated other comprehensive loss	(60,134)	(63,394)
Total NuStar Energy L.P. partners' equity	1,768,645	1,902,136
Noncontrolling interest	—	1,658
Total partners' equity	1,768,645	1,903,794
Total liabilities and partners' equity	$4,877,367	$5,032,186

See Condensed Notes to Consolidated Financial Statements.

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Revenues:				
Service revenues	$266,651	$243,712	$755,551	$700,922
Product sales	527,771	534,433	1,637,829	1,977,423
Total revenues	794,422	778,145	2,393,380	2,678,345
Costs and expenses:				
Cost of product sales	509,794	527,217	1,578,508	1,928,237
Operating expenses:				
Third parties	84,570	87,025	246,541	248,493
Related party	31,394	30,076	91,025	93,440
Total operating expenses	115,964	117,101	337,566	341,933
General and administrative expenses:				
Third parties	7,567	8,336	20,044	24,171
Related party	17,400	10,495	48,942	41,807
Total general and administrative expenses	24,967	18,831	68,986	65,978
Depreciation and amortization expense	48,599	46,245	142,765	133,116
Total costs and expenses	699,324	709,394	2,127,825	2,469,264
Operating income	95,098	68,751	265,555	209,081
Equity in earnings (loss) of joint ventures	2,749	(5,358)	1,737	(26,629)
Interest expense, net	(33,007)	(30,823)	(100,546)	(92,849)
Interest income from related party	—	1,828	1,055	4,560
Other (expense) income, net	(1,388)	1,389	1,816	3,917
Income from continuing operations before income tax expense	63,452	35,787	169,617	98,080
Income tax expense	4,335	105	10,317	8,087
Income from continuing operations	59,117	35,682	159,300	89,993
Income (loss) from discontinued operations, net of tax	2,831	(2,446)	(2,316)	616
Net income	61,948	33,236	156,984	90,609
Less net loss attributable to noncontrolling interest	(173)	(161)	(395)	(439)
Net income attributable to NuStar Energy L.P.	$62,121	$33,397	$157,379	$91,048
Net income (loss) per unit applicable to limited partners:				
Continuing operations	$0.61	$0.31	$1.59	$0.71
Discontinued operations	0.03	(0.03)	(0.03)	0.02
Total (Note 10)	$0.64	$0.28	$1.56	$0.73
Weighted-average limited partner units outstanding	77,886,078	77,886,078	77,886,078	77,886,078
Comprehensive income	$58,167	$38,790	$159,811	$90,042
Less comprehensive loss attributable to noncontrolling interest	(159)	(729)	(828)	(2,206)
Comprehensive income attributable to NuStar Energy L.P.	$58,326	$39,519	$160,639	$92,248

See Condensed Notes to Consolidated Financial Statements.

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

	Nine Months Ended September 30,	
	2014	2013
Cash Flows from Operating Activities:		
Net income	$156,984	$90,609
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization expense	142,765	137,185
Amortization of debt related items	7,015	1,721
Gain from sale or disposition of assets	(3,840)	(8,739)
Asset impairment loss	2,067	—
Deferred income tax expense (benefit)	2,453	(3,815)
Equity in (earnings) loss of joint ventures	(1,737)	26,629
Distributions of equity in earnings of joint ventures	5,879	5,787
Changes in current assets and current liabilities (Note 11)	1,080	116,838
Other, net	2,529	12,325
Net cash provided by operating activities	315,195	378,540
Cash Flows from Investing Activities:		
Capital expenditures	(229,548)	(260,701)
Change in accounts payable related to capital expenditures	10,910	(2,879)
Proceeds from sale or disposition of assets	25,975	116,467
Increase in note receivable from related party	(13,328)	(50,761)
Other, net	(853)	156
Net cash used in investing activities	(206,844)	(197,718)
Cash Flows from Financing Activities:		
Proceeds from long-term debt borrowings	537,436	1,299,220
Proceeds from note offering, net of issuance costs	—	687,151
Proceeds from short-term debt borrowings	205,200	—
Long-term debt repayments	(451,269)	(1,897,182)
Short-term debt repayments	(183,800)	—
Distributions to unitholders and general partner	(294,153)	(294,153)
Payments for termination of interest rate swaps	—	(33,697)
Other, net	2,540	3,168
Net cash used in financing activities	(184,046)	(235,493)
Effect of foreign exchange rate changes on cash	638	(4,412)
Net decrease in cash and cash equivalents	(75,057)	(59,083)
Cash and cash equivalents as of the beginning of the period	100,743	83,602
Cash and cash equivalents as of the end of the period	$25,686	$24,519

See Condensed Notes to Consolidated Financial Statements.

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NUSTAR ENERGY L.P. AND SUBSIDIARIES
CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. ORGANIZATION AND BASIS OF PRESENTATION

Organization and Operations
NuStar Energy L.P. (NuStar Energy) (NYSE: NS) is engaged in the transportation of petroleum products and anhydrous ammonia, the terminalling and storage of petroleum products and the marketing of petroleum products. Unless otherwise indicated, the terms "NuStar Energy," "the Partnership," "we," "our" and "us" are used in this report to refer NuStar Energy L.P., to one or more of our consolidated subsidiaries or to all of them taken as a whole. NuStar GP Holdings, LLC (NuStar GP Holdings) (NYSE: NSH) owns our general partner, Riverwalk Logistics, L.P., and owns a 15.1% total interest in us as of September 30, 2014.

We conduct our operations through our subsidiaries, primarily NuStar Logistics, L.P. (NuStar Logistics) and NuStar Pipeline Operating Partnership L.P. (NuPOP). We have three business segments: pipeline, storage and fuels marketing.

Basis of Presentation
These unaudited condensed consolidated financial statements include the accounts of the Partnership and subsidiaries in which the Partnership has a controlling interest. Noncontrolling interests are separately disclosed on the financial statements. Inter-partnership balances and transactions have been eliminated in consolidation. We account for our investments in joint ventures using the equity method of accounting.

These unaudited condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles (GAAP) for interim financial information and with the instructions to the Quarterly Report on Form 10-Q and Article 10 of Regulation S-X of the Securities Exchange Act of 1934. Accordingly, they do not include all of the information and notes required by GAAP for complete consolidated financial statements. In the opinion of management, all adjustments considered necessary for a fair presentation have been included, and all disclosures are adequate. All such adjustments are of a normal recurring nature unless disclosed otherwise. Financial information for the three and nine months ended September 30, 2014 and 2013 included in these Condensed Notes to Consolidated Financial Statements is derived from our unaudited condensed consolidated financial statements. Operating results for the three and nine months ended September 30, 2014 are not necessarily indicative of the results that may be expected for the year ending December 31, 2014. The consolidated balance sheet as of December 31, 2013 has been derived from the audited consolidated financial statements as of that date. These unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2013.

New Accounting Pronouncements
In May 2014, the Financial Accounting Standards Board (FASB) and the International Accounting Standards Board jointly issued a comprehensive new revenue recognition standard. The standard is effective for public entities for annual and interim periods beginning after December 15, 2016, using one of two retrospective transition methods. Early adoption is not permitted for public entities. We are currently assessing the impact of this new guidance on our financial statements and disclosures, and we have not yet selected a transition method.

In April 2014, the FASB amended the disclosure requirements for discontinued operations. Under the amended guidance, a discontinued operation is defined as the disposal of a component that represents a strategic shift that has (or will have) a major effect on an entity's operations and financial results. The amended guidance also requires expanded disclosures about discontinued operations and disposals of a significant part of an entity that do not qualify as discontinued operations. The amended guidance is effective prospectively to new disposals and new classifications of assets held for sale in annual periods beginning after December 15, 2014, and interim periods within those annual periods. Accordingly, we plan to adopt the amended guidance January 1, 2015.

2. DISPOSITIONS AND DISCONTINUED OPERATIONS

Dispositions

On February 26, 2014, we sold our remaining 50% ownership interest in NuStar Asphalt LLC to Lindsay Goldberg LLC (Lindsay Goldberg), a private investment firm (the Asphalt JV Sale). Effective February 27, 2014, NuStar Asphalt LLC changed its name to Axeon Specialty Products LLC (Axeon). Lindsay Goldberg now owns 100% of Axeon. As a result of the Asphalt JV Sale, we ceased applying the equity method of accounting. Upon completion of the Asphalt JV Sale, the parties agreed to: (i) convert the $250.0 million unsecured revolving credit facility provided by us to Axeon (the NuStar JV Facility) from a revolving credit agreement into a $190.0 million term loan (the Axeon Term Loan); (ii) terminate the terminal services agreements with respect to our terminals in Rosario, NM, Catoosa, OK and Houston, TX; (iii) amend the terminal services agreements for our terminals in Baltimore, MD and Jacksonville, FL; and (iv) transfer ownership of both the Wilmington, NC and Dumfries, VA terminals to Axeon, which were categorized as assets held for sale at December 31, 2013. See Note 8 for a discussion of our agreements with Axeon.

Discontinued Operations

Terminals Held for Sale. In addition to the terminals located in Wilmington, NC and Dumfries, VA, we have identified and plan to divest several non-strategic, underperforming terminal facilities. As a result, we have classified the associated property, plant and equipment as "Assets held for sale" on the consolidated balance sheets. We presented the results of operations for those facilities, which were previously reported in the storage segment, as discontinued operations for all periods presented. In September 2014, we sold our 75% interest in our facility in Mersin, Turkey for total proceeds of $13.4 million. We recognized a gain of $3.7 million, which is included in discontinued operations for the three and nine months ended September 30, 2014. In June 2014, we sold three terminals located in Mobile, AL with an aggregate storage capacity of 1.8 million barrels for total proceeds of $13.7 million. We allocated interest expense to discontinued operations based on the ratio of net assets discontinued to consolidated net assets as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
	(Thousands of Dollars)			
Allocated interest expense	$115	$352	$811	$1,056

San Antonio Refinery. On January 1, 2013, we sold our fuels refinery in San Antonio, Texas (the San Antonio Refinery) and related assets for approximately $117.0 million (the San Antonio Refinery Sale). We recognized a gain of $9.3 million on the sale, which is included in discontinued operations for the nine months ended September 30, 2013.

The following table summarizes the results from discontinued operations:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
	(Thousands of Dollars)			
Revenues	$276	$1,865	$3,456	$5,756
Income (loss) before income tax expense	$2,831	$(3,114)	$(2,316)	$(1,324)

3. INVENTORIES

Inventories consisted of the following:

	September 30, 2014	December 31, 2013
	(Thousands of Dollars)	
Crude oil	$6,294	$6,485
Finished products	102,602	123,656
Materials and supplies	9,041	8,006
Total	$117,937	$138,147

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4. DEBT

Revolving Credit Agreement
During the nine months ended September 30, 2014, the balance under our $1.5 billion five-year revolving credit agreement (the 2012 Revolving Credit Agreement) increased by $79.4 million, which we used for general partnership purposes. The 2012 Revolving Credit Agreement bears interest, at our option, based on either an alternative base rate, a LIBOR-based rate or a EURIBOR-based rate. The interest rate on the 2012 Revolving Credit Agreement is subject to adjustment if our debt rating is downgraded (or upgraded) by certain credit rating agencies. As of September 30, 2014, our weighted average interest rate was 2.2% and we had $582.4 million outstanding.

The 2012 Revolving Credit Agreement contains customary restrictive covenants, such as limitations on indebtedness, liens, mergers, asset transfers and certain investing activities. In addition, the 2012 Revolving Credit Agreement requires us to maintain, as of the end of each rolling period, which consists of any period of four consecutive fiscal quarters, a consolidated debt coverage ratio (consolidated debt to consolidated EBITDA, each as defined in the 2012 Revolving Credit Agreement) not to exceed 5.00-to-1.00. The requirement not to exceed a maximum consolidated debt coverage ratio may limit the amount we can borrow under the 2012 Revolving Credit Agreement to an amount less than the total amount available for borrowing. As of September 30, 2014, our consolidated debt coverage ratio was 4.0x, and we had $839.1 million available for borrowing.

On October 29, 2014, we amended and restated the 2012 Revolving Credit Agreement primarily to reduce the interest rate, to extend the maturity to October 29, 2019 and to amend certain of the restrictive covenants.

Gulf Opportunity Zone Revenue Bonds
In 2008, 2010 and 2011, the Parish of St. James, Louisiana issued, pursuant to the Gulf Opportunity Zone Act of 2005, tax-exempt revenue bonds (the GoZone Bonds) associated with our St. James, Louisiana terminal expansions. The GoZone Bonds bear interest based on a weekly tax-exempt bond market interest rate, and we pay interest monthly. The interest rate was 0.1% as of September 30, 2014. Following the issuance, the proceeds were deposited with a trustee and are disbursed to us upon our request for reimbursement of expenditures related to our St. James terminal expansions. We include the amount remaining in trust in “Other long-term assets, net,” and we include the amount of bonds issued in “Long-term debt” on the consolidated balance sheets. For the nine months ended September 30, 2014, we received $0.8 million from the trustee. As of September 30, 2014, the amount remaining in trust totaled $82.7 million.

Short-term Lines of Credit
In 2014, we entered into two short-term line of credit agreements with an aggregate uncommitted borrowing capacity of up to $80.0 million. These agreements allow us to better manage the fluctuations in our daily cash requirements and minimize our excess cash balances. The interest rate and maturity vary and are determined at the time of the borrowing. We had $21.4 million outstanding under these short-term lines of credit as of September 30, 2014.

5. COMMITMENTS AND CONTINGENCIES

Contingencies
We have contingent liabilities resulting from various litigation, claims and commitments. We record accruals for loss contingencies when losses are considered probable and can be reasonably estimated. Legal fees associated with defending the Partnership in legal matters are expensed as incurred. As of September 30, 2014, we have accrued $1.1 million for contingent losses. The amount that will ultimately be paid may differ from the recorded accruals, and the

timing of such payments is uncertain. In addition, due to the inherent uncertainty of litigation, there can be no assurance that the resolution of any particular claim or proceeding would not have a material adverse effect on our results of operations, financial position or liquidity.

6. FAIR VALUE MEASUREMENTS

We segregate the inputs used in measuring fair value into three levels: Level 1, defined as observable inputs such as quoted prices for identical assets or liabilities in active markets; Level 2, defined as inputs other than quoted prices in active markets that are either directly or indirectly observable, such as quoted prices for similar assets or liabilities in active markets or quoted prices for identical assets or liabilities in markets that are not active; and Level 3, defined as unobservable inputs in which little or no market data exists. We consider counterparty credit risk and our own credit risk in the determination of all estimated fair values.

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

Recurring Fair Value Measurements
The following assets and liabilities are measured at fair value on a recurring basis:

	September 30, 2014			
	Level 1	Level 2	Level 3	Total
	(Thousands of Dollars)			
Assets:				
Other current assets:				
Product imbalances	$2,822	$—	$—	$2,822
Commodity derivatives	6,714	3,166	—	9,880
Other long-term assets, net:				
Commodity derivatives	—	233	—	233
Total	$9,536	$3,399	$—	$12,935
Liabilities:				
Accrued liabilities:				
Product imbalances	$(2,335)	$—	$—	$(2,335)
Commodity derivatives	—	(1,615)	—	(1,615)
Other long-term liabilities:				
Commodity derivatives	—	(105)	—	(105)
Guarantee liability	—	—	(1,730)	(1,730)
Total	$(2,335)	$(1,720)	$(1,730)	$(5,785)

	December 31, 2013			
	Level 1	Level 2	Level 3	Total
	(Thousands of Dollars)			
Assets:				
Other current assets:				
Product imbalances	$1,980	$—	$—	$1,980
Commodity derivatives	—	4,948	—	4,948
Other long-term assets, net:				
Commodity derivatives	—	6,977	—	6,977
Total	$1,980	$11,925	$—	$13,905
Liabilities:				
Accrued liabilities:				
Product imbalances	$(2,190)	$—	$—	$(2,190)
Commodity derivatives	(1,433)	(800)	—	(2,233)
Contingent consideration	—	—	(1,318)	(1,318)
Other long-term liabilities:				
Commodity derivatives	—	(1,575)	—	(1,575)
Guarantee liability	—	—	(1,880)	(1,880)
Total	$(3,623)	$(2,375)	$(3,198)	$(9,196)

Product Imbalances. We value our assets and liabilities related to product imbalances using quoted market prices in active markets as of the reporting date.

Commodity Derivatives. We base the fair value of certain of our commodity derivative instruments on quoted prices on an exchange; accordingly, we include these items in Level 1 of the fair value hierarchy. We also have derivative instruments for which we determine fair value using industry pricing services and other observable inputs, such as quoted prices on an exchange for similar derivative instruments. Therefore, we include these derivative instruments in Level 2 of the fair value hierarchy. See Note 7 for a discussion of our derivative instruments.

Contingent Consideration. On December 13, 2012, NuStar Logistics acquired certain assets from TexStar Midstream Services, LP and certain of its affiliates (collectively, TexStar) for approximately $325.0 million (the TexStar Asset Acquisition), including contingent consideration. In connection with the TexStar Asset Acquisition, we could have been obligated to pay additional consideration to TexStar, depending upon the cost of work required to complete certain assets and obtain outstanding real estate rights (collectively, the Contingent Consideration). In August 2014, we settled with TexStar and reduced the associated liability to $0.

Guarantees. As of September 30, 2014, we recorded a liability of $1.7 million representing the fair value of guarantees we have issued on behalf of Axeon. We estimated the fair value considering the probability of default by Axeon and an estimate of the amount we would be obligated to pay under the guarantees at the time of default. We calculated the fair value based on the guarantees outstanding as of September 30, 2014, totaling $73.3 million, plus two guarantees that do not specify a maximum amount. Our estimate of the fair value is based on significant inputs not observable in the market and thus falls within Level 3 of the fair value hierarchy. See Note 8 for a discussion of our agreements with Axeon.

In the event we are obligated to perform under any of these guarantees, the amount paid by us will be treated as additional borrowings under the Axeon Term Loan. As a result, we increased the carrying value of the note receivable from Axeon by the same amount as the increase to the liability for the fair value of the guarantees outstanding as of September 30, 2014.

The following table summarizes the activity in our Level 3 liabilities:

	Nine Months Ended September 30, 2014	
	(Thousands of Dollars)	
Beginning balance	$3,198	
Amounts settled	(870	)
Adjustments to guarantee liability	(150	)
Changes in fair value recorded in earnings:		
Operating expenses	(448	)
Ending balance	$1,730	

Non-recurring Fair Value Measurements

We classified the property, plant and equipment associated with certain terminals as “Assets held for sale” on the consolidated balance sheet and recorded those assets at fair value, less costs to sell. We estimated the fair values of $2.3 million and $22.0 million as of September 30, 2014 and December 31, 2013, respectively, using a weighted-average of values calculated using an income approach and a market approach. The income approach calculates fair value by discounting the estimated net cash flows generated by the related terminal. The market approach involves estimating the fair value measurement on an earnings multiple based on public company transaction data. Our estimate of the fair value is based on significant inputs not observable in the market and thus falls within Level 3 of the fair value hierarchy.

Fair Value of Financial Instruments

We recognize cash equivalents, receivables, note receivables, payables and debt in our consolidated balance sheets at their carrying amounts. The fair values of these financial instruments, except for a note receivable from Axeon and long-term debt, approximate their carrying amounts. The estimated fair value and carrying amounts of the debt and note receivable were as follows:

	September 30, 2014		December 31, 2013	
	Fair Value	Carrying Amount	Fair Value	Carrying Amount
	(Thousands of Dollars)			
Long-term debt	$2,783,666	$2,731,551	$2,636,734	$2,655,553
Note receivable from Axeon	$148,300	$170,385	$133,416	$165,440

We estimated the fair value of our publicly-traded senior notes based upon quoted prices in active markets; therefore, we determined that the fair value of our publicly traded senior notes falls in Level 1 of the fair value hierarchy. For our other debt, for which a quoted market price is not available, we estimated the fair value using a discounted cash flow analysis using current incremental borrowing rates for similar types of borrowing arrangements and determined that the fair value falls in Level 2 of the fair value hierarchy.

The carrying amount of the Axeon Term Loan is $170.4 million, consisting of the following: (i) the outstanding principal amount of $190.0 million; (ii) plus the fair value of guarantees of $1.7 million as of September 30, 2014 (iii) less equity losses from our investment in Axeon of $21.3 million incurred prior to the Asphalt JV Sale and after the carrying value of our equity investment in Axeon was reduced to zero. We review the financial information of Axeon monthly for possible non-payment indicators.

We estimated the fair value of the note receivable using discounted cash flows, which use observable inputs such as time to maturity and market interest rates, and determined the fair value falls in Level 2 of the fair value hierarchy. See Note 8 for additional information on the note receivable from Axeon.

7. DERIVATIVES AND RISK MANAGEMENT ACTIVITIES

We utilize various derivative instruments to manage our exposure to commodity price risk and interest rate risk. Our risk management policies and procedures are designed to monitor interest rates, futures and swap positions and over-the-counter positions, as well as physical volumes, grades, locations and delivery schedules, to help ensure that our hedging activities address our market risks. Our risk management committee oversees our trading controls and procedures and certain aspects of commodity and trading risk management. Our risk management committee also reviews all new commodity and trading risk management strategies in accordance with our risk management policy, as approved by our board of directors.

Interest Rate Risk

As of September 30, 2014, we had no forward-starting interest rate swap agreements. However, we previously entered into certain interest rate swap agreements to manage our exposure to changes in interest rates, which included forward-starting interest rate swap agreements. These swaps qualified, and we designated them, as cash flow hedges. In 2013, we terminated our remaining forward-starting interest rate swap agreements. We recorded the effective portion of mark-to-market adjustments as a component of “Accumulated other comprehensive loss.” The amount in accumulated other comprehensive income (OCI) is amortized into “Interest expense, net” as the interest payments occur or expensed immediately if the interest payments are probable not to occur.

Commodity Price Risk

We are exposed to market risks related to the volatility of crude oil and refined product prices. In order to reduce the risk of commodity price fluctuations with respect to our crude oil and finished product inventories and related firm commitments to purchase and/or sell such inventories, we utilize commodity futures and swap contracts, which qualify and we designate as fair value hedges. Derivatives that are intended to hedge our commodity price risk, but fail to qualify as fair value or cash flow hedges, are considered economic hedges, and we record associated gains and losses in net income.

The volume of commodity contracts is based on open derivative positions and represents the combined volume of our long and short open positions on an absolute basis, which totaled 15.6 million barrels and 15.2 million barrels as of September 30, 2014 and December 31, 2013, respectively.

As of December 31, 2013, we had $3.3 million of margin deposits related to our derivative instruments and none as of September 30, 2014.

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

The fair values of our derivative instruments included in our consolidated balance sheets were as follows:

	Balance Sheet Location	Asset Derivatives September 30, 2014	Asset Derivatives December 31, 2013	Liability Derivatives September 30, 2014	Liability Derivatives December 31, 2013
		(Thousands of Dollars)			
Derivatives Designated as Hedging Instruments:					
Commodity contracts	Other current assets	$470	$—	$(63)	$—
Commodity contracts	Accrued liabilities	—	—	—	(130)
Derivatives Not Designated as Hedging Instruments:					
Commodity contracts	Other current assets	25,508	16,168	(16,035)	(11,220)
Commodity contracts	Other long-term assets, net	1,754	15,883	(1,521)	(8,906)
Commodity contracts	Accrued liabilities	2,807	4,523	(4,422)	(6,626)
Commodity contracts	Other long-term liabilities	246	5,448	(351)	(7,023)
Total		30,315	42,022	(22,329)	(33,775)
Total Derivatives		$30,785	$42,022	$(22,392)	$(33,905)

Certain of our derivative instruments are eligible for offset in the consolidated balance sheets and subject to master netting arrangements. Under our master netting arrangements, there is a legally enforceable right to offset amounts, and we intend to settle such amounts on a net basis. The following are the net amounts presented on the consolidated balance sheets:

Commodity Contracts	September 30, 2014	December 31, 2013
	(Thousands of Dollars)	
Net amounts of assets presented in the consolidated balance sheets	$10,113	$11,925
Net amounts of liabilities presented in the consolidated balance sheets	$(1,720)	$(3,808)

The earnings impact of our derivative activity was as follows:

Derivatives Designated as Fair Value Hedging Instruments	Income Statement Location	Amount of Gain (Loss) Recognized in Income on Derivative (Effective Portion)	Amount of Gain (Loss) Recognized in Income on Hedged Item	Amount of Gain (Loss) Recognized in Income on Derivative (Ineffective Portion)
		(Thousands of Dollars)		
Three months ended September 30, 2014:				
Commodity contracts	Cost of product sales	$1,219	$(1,058)	$ 161
Three months ended September 30, 2013:				
Commodity contracts	Cost of product sales	$(3,853)	$4,184	$ 331

Nine months ended September 30, 2014: