

STAR GAS PARTNERS LP  
Form 424B5  
April 07, 2006  
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Filed pursuant to Rule 424(b)(5)  
Registration No. 333-131098

**PROSPECTUS**

**STAR GAS PARTNERS, L.P.**

**Rights Offering For**

**19,687,500 Common Units**

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We are distributing to our common unitholders non-transferable subscription rights to purchase our common units. The holder of record of each common unit held at the close of business on April 6, 2006, the record date for the distribution, is being issued .6121 rights to purchase one common unit. Each full right is exercisable to purchase one common unit at \$2.00 per unit.

If all rights are exercised, we will receive approximately \$39.375 million from the rights offering, before paying estimated expenses of approximately \$6.5 million in connection with the strategic recapitalization of Star Gas Partners described below. We will not issue fractional units or pay cash in lieu thereof. Instead, we will round the total number of units each rightsholder is entitled to acquire upward to the nearest whole unit. The subscription price for units may be paid only in cash. All exercises of rights are irrevocable. No rightsholder will have the right to oversubscribe.

We have entered into a unit purchase agreement dated December 5, 2006, as amended on March 12, 2006 and March 30, 2006 (the "unit purchase agreement") with Kestrel Energy Partners, LLC ("Kestrel") and its wholly owned subsidiaries, KM2, LLC ("M2") and Kestrel Heat, LLC ("Kestrel Heat"). Pursuant to the unit purchase agreement, M2 agreed to purchase 6,250,000 common units and Kestrel Heat agreed to purchase 500,000 common units, at a purchase price of \$2.50 per unit for an aggregate purchase price of \$16.875 million. M2 also agreed to provide a standby commitment to purchase an additional number of common units equal to the number of common units not purchased in the rights offering, at a purchase price of \$2.25 per unit. Upon the closing of the transactions contemplated by the unit purchase agreement, Star Gas LLC, our current general partner ("Star Gas"), will withdraw and, as approved by our unitholders, Kestrel Heat will replace Star Gas as our new general partner.

The rights offering, together with M2's standby commitment, are part of a strategic recapitalization of Star Gas Partners that has been approved by our unitholders which, if completed, would result in a reduction in the outstanding amount of our 10.25% senior notes due 2013 ("senior notes") of up to \$100 million (assuming full noteholder participation in the senior notes tender offer described below) and the issuance of approximately 43,608,808 new common units.

The rights offering will expire at 5:00 p.m., New York City time, on April 25, 2006, or such later date and time to which the rights offering is extended (the "Expiration Time"). **NO EXERCISES OF RIGHTS WILL BE ACCEPTED FOLLOWING THE EXPIRATION TIME.** Unitholders who have exercised their rights pursuant to the rights offering may NOT revoke or withdraw their exercise of their rights. We may terminate the rights offering for any reason before the Expiration Time. Unless we terminate the rights offering, we will issue the units purchased by you in the rights offering as soon as practicable following the Expiration Time. LaSalle Bank National Association is the subscription agent for the rights offering. We have not employed any brokers, dealers or underwriters in connection with the rights offering.

Our common units are listed under the symbol **SGU** on The New York Stock Exchange. On April 5, 2006, the closing sales price per common unit was \$2.61. The rights are non-transferable and will not be listed on any exchange.

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**This investment involves risks. Before making an investment, carefully consider the Risk Factors beginning on page 32 of this prospectus.**

**Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.**

Our unitholders have approved the proposals necessary to implement the recapitalization transaction and the completion thereof.

**Neither we nor the board of directors of our general partner has made any recommendation as to whether you should exercise your rights. You should decide whether to subscribe for common units or simply take no action with respect to your rights, based upon your own assessment of the risks in making an additional investment in us. See **Risk Factors, The Rights Offering No Recommendations to Rightsholders, Information Regarding Kestrel Heat Interests of the Proposed Executive Officers and Directors in the Recapitalization and Conflicts of Interest.****

We may amend or supplement this prospectus from time to time by filing amendments or supplements as required. You should read this entire prospectus and any amendments or supplements to this prospectus carefully before making your investment decision.

**The date of this prospectus is April 6, 2006.**

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**GUIDE TO READING THIS PROSPECTUS**

Certain of the information contained in this prospectus was obtained from other sources. This prospectus also incorporates by reference important business and financial information about us that is not included in or delivered with this prospectus.

You should rely only on the information contained in this prospectus or any supplement and any information incorporated by reference in this prospectus or any supplement. We have not authorized anyone to provide you with any information that is different from such information. If you receive any unauthorized information, you should not rely on it. You should disregard anything we said in an earlier document that is inconsistent with what is included or incorporated by reference in this prospectus or any supplement.

You should not assume that the information in this prospectus or any supplement is current as of any date other than the date on the front page of this prospectus or on the date of any supplement as to information contained in it. This prospectus is not an offer to sell nor is it seeking an offer to buy these securities in any state or jurisdiction where the offer or sale is not permitted.

We include cross references to captions in this prospectus where you can find further related discussions. The above table of contents tells you where to find these captions.

Throughout this prospectus, we refer to ourselves, Star Gas Partners, L.P. together with our subsidiaries, as we or us or Star Gas Partners. We sometimes refer to the board of directors of our current general partner, Star Gas, as our board of directors, our board, the board, Star Gas board or Star Gas Partners board.

For ease of reference, a glossary of some terms used in this prospectus is included as Annex B to this prospectus. Capitalized terms not otherwise defined in this prospectus have the meanings given in the glossary.

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**FORWARD-LOOKING STATEMENTS**

Many of the statements contained in this prospectus, including, without limitation, statements regarding our business strategy, plans and objectives of our management for future operations are forward-looking within the meaning of the federal securities laws. These statements use forward-looking words, such as anticipate, continue, expect, may, will, estimate, believe or other similar words. These statements, including those contained in Prospectus Summary 2006 Forecast of Star Gas Partners, discuss future expectations or contain projections. Although we believe that the expectations reflected in the forward-looking statements are reasonable, actual results may differ from those suggested by the forward-looking statements for various reasons, including:

the closing of the recapitalization;

the effect of weather conditions on our financial performance;

anticipated proceeds from weather insurance;

the price and supply of home heating oil;

the consumption patterns of our customers;

our ability to obtain satisfactory gross profit margins;

our ability to obtain new customers and retain existing customers;

our ability to effect strategic acquisitions or redeploy underperforming assets;

the ultimate disposition of excess proceeds from the sale of the propane segment should the recapitalization not be consummated;

the impact of litigation;

the ongoing impact of the business process redesign project at the heating oil segment and our ability to address issues related to that project;

natural gas conversions;

future union relations and the outcome of current and future union negotiations;

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the impact of current and future environmental, health and safety regulations;

customer creditworthiness; and

marketing plans.

The above factors, as well as the factors set forth below under Risk Factors, could cause our actual results to differ materially from those contained in any forward-looking statement. We disclaim any obligation to update the above list or to announce publicly the result of any revisions to any of the forward-looking statements to reflect future events or developments.

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**PROSPECTUS SUMMARY**

*This summary information is to help you understand our company and the rights offering. It may not contain all the information that may be important to you. You should carefully read this prospectus and the documents incorporated by reference to understand fully our common units, as well as the tax and other considerations that are important to you in making your investment decision. You should pay special attention to the Risk Factors section beginning on page 32 of this prospectus to determine whether an investment in our common units is appropriate for you.*

**Who We Are**

**Star Gas Partners, L.P.**

We are the largest retail distributor of home heating oil in the United States, based on volume as reported by the National Oilheat Research Alliance Organization, March 2003. As of March 31, 2006, our home heating oil operations serve approximately 455,000 customers in the Northeast and Mid-Atlantic regions. For the twelve months ended December 31, 2005, our home heating oil segment sold 476.3 million gallons of home heating oil. We were also formerly engaged as a retail distributor of propane until December 17, 2004, when we sold our propane segment.

For the twelve months ended December 31, 2005, approximately 76% of total sales from our heating oil operations were from sales of home heating oil, approximately 14% were from the installation and repair of heating and air conditioning equipment and approximately 10% were from the sale of other petroleum products, including diesel fuel and gasoline, primarily to commercial customers for fleet fuel service. During this period, our home heating oil operations generated total sales of approximately \$1.3 billion.

Our executive offices are located at 2187 Atlantic Street, Stamford, Connecticut 06902. The telephone number is (203) 328-7310.

**Recent Results**

The following is a summary of our results of operations for the three months ended December 31, 2005. For a more detailed discussion of our results of operations for this period, see our Quarterly Report on Form 10-Q for the three months ended December 31, 2005, as amended by Form 10-Q/A (the Quarterly Report on Form 10-Q/A ), which is incorporated by reference in this prospectus.

*Volume:* For the three months ended December 31, 2005, retail volume of home heating oil declined by 11.0 million gallons, or 7.7%, to 131.3 million gallons, as compared to 142.3 million gallons for the three months ended December 31, 2004. We believe that this 11.0 million gallon home heating oil decline was due almost entirely to net customer attrition, which occurred in fiscal 2005 and continued through the fiscal first quarter of 2006. Net customer attrition is the difference between gross customer losses and customers added through internal marketing efforts. Customers added through acquisitions do not impact the calculation of net customer attrition. For both fiscal 2005 and the twelve months ended December 31, 2005, the heating oil segment experienced net customer attrition of approximately 7.1% and 8.3%, respectively. Temperatures in our geographic areas of operations for the three months ended December 31, 2005 were approximately equal to the three

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months ended December 31, 2004 and approximately 2.4% warmer than normal, as reported by the National Oceanic Atmospheric Administration ( NOAA ). Due to the significant increase in the price per gallon of home heating oil, we believe that customers are using less home heating oil given similar temperatures when compared to prior periods. Indications based on internal studies suggested that in fiscal 2005, customers reduced their consumption by approximately 4.4%. We cannot determine if conservation is a permanent or temporary phenomenon.



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*Operating Income (Loss):* For the three months ended December 31, 2005, operating income increased \$41.4 million to \$20.4 million, as compared to a loss of \$21.0 million in operating income for the three months ended December 31, 2004. This increase was due to an increase in product gross profit margin of \$22.7 million, improvements in net service and installation profitability of \$2.6 million, lower bridge and financing expenses of \$10.4 million and a reduction in marketing expenses of \$3.7 million.

*Income (Loss) From Continuing Operations:* For the three months ended December 31, 2005, income (loss) from continuing operations increased \$87.5 million to \$12.9 million, as compared to a loss of \$74.6 million for the three months ended December 31, 2004. This increase was due to the \$41.4 million increase in operating income, lower interest expense of \$3.3 million and higher interest income of \$0.5 million. The quarter-to-quarter comparison was also favorably impacted by the \$42.1 million loss on redemption of debt recorded in the three months ended December 31, 2004.

*Net Income:* For the three months ended December 31, 2005, net income declined by \$61.9 million, to \$12.5 million, as compared to \$74.4 million in net income for the three months ended December 31, 2004, as an \$87.5 million increase in income from continuing operations and a \$4.6 million increase in income from discontinued operations in the 2006 first fiscal quarter was offset by a \$153.6 million gain on the sale of the propane segment recorded in the year ago period.

*Three months ended March 31, 2006:* For the three months ended March 31, 2006, retail volume of home heating oil declined by an estimated 61.7 million gallons, or 25.2%, to 183.3 million gallons, as compared to 245.0 million gallons for the three months ended March 31, 2005. We believe that this decline was due to net customer attrition, conservation and the impact of warmer temperatures. Based on estimates, we believe that temperatures were approximately 15% warmer for the three months ended March 31, 2006, as compared to the three months ended March 31, 2005. We expect that home heating oil volume sold for the remainder of fiscal 2006 will be substantially less than in the comparable period in fiscal 2005 due to net customer attrition, conservation and other factors such as delivery scheduling.

Due to the decline in retail home heating oil volume, we believe that our results for the three months ended March 31, 2006 when compared to the three months ended March 31, 2005 will be adversely impacted. Due to the fixed nature of certain branch and delivery expenses, we expect that these expenses will increase when measured on a per gallon basis. During the three months ended March 31, 2006, we lost approximately 9,800 accounts (net) or 2.2% of our home heating oil customer base, as compared to the three months ended March 31, 2005 in which we lost 9,900 accounts (net) or 2.0% of our home heating oil customer base.

## **2006 Business Outlook**

We expect our business to continue to be affected by the following key trends. Our expectations are based on assumptions made by us, and information currently available to us. To the extent our underlying assumptions about, or interpretations of, available information prove to be incorrect, our actual results may vary materially from our expected results. See Risk Factors.

We face numerous challenges in fiscal 2006. In particular, it will be difficult to stem the high attrition rates that we are currently experiencing, primarily as a result of a volatile and consistently high heating oil prices in the commodity markets.

We believe global demand for oil and gas is expected to increase in 2006, particularly as a result of emerging energy consumers such as China and India. This resultant increase in demand would likely continue to support relatively high commodity prices.



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We believe that our efforts to decentralize a portion of our current service operations by redirecting a portion of our customer calls and empowering our local branches will provide benefits in stemming attrition rates in 2006. In addition, we believe our cost control programs, coupled with our discipline in hedging rising commodity price risk for our price protected customer contracts and continued philosophy of maintaining reasonable margins in spite of competitors' aggressive price tactics, should mitigate the effect of the attrition associated with the continued high heating oil prices in fiscal 2006. As a result we anticipate that our per-gallon margin will improve over our margins earned in fiscal 2005.

Our ability to satisfy our liquidity and capital requirements will depend on our future performance, which will be subject to prevailing economic, financial, business and weather conditions, the ability to pass on the full impact of high wholesale heating oil prices to customers, the effects of high customer attrition, conservation and other factors, most of which are beyond our control. See **Risk Factors**. Capital requirements, at least in the near term, are expected to be provided by cash flows from operating activities, cash on hand at December 31, 2005 or a combination thereof. To the extent future capital requirements exceed cash flows from operating activities, we anticipate that working capital will be financed by our revolving credit facility as discussed below and repaid from subsequent seasonal reductions in inventory and accounts receivable. We believe the proposed recapitalization described below, which has been approved by our unitholders, if completed, will substantially strengthen our balance sheet and thereby assist us in meeting our liquidity and capital requirements. We also believe we will be able to operate more efficiently going forward with less long-term debt.

In the latter part of fiscal 2006, we intend to pursue asset acquisitions, to the extent permitted in our credit facility, in geographic areas that will enable us to realize margins we consider reasonable in the face of aggressive localized price competition as one way to replace volume lost through attrition. In addition, we may dispose of operations in markets where we are not able to effectively employ our strategy of maintaining reasonable margins. We anticipate using internally generated cash flow, in part, to the extent permitted under our credit facility and senior note indenture, to fund acquisitions.

## **The Recapitalization**

The rights offering is an integral part of a strategic recapitalization of Star Gas Partners approved by our board of directors and our unitholders. If completed, the recapitalization would result in a reduction in the outstanding amount of our senior notes of up to \$100 million (assuming full noteholder participation in the senior notes tender offer described below under **Noteholder Agreements**) and the issuance of approximately 43,608,808 new common units.

The closing of the rights offering is conditioned upon the simultaneous closing of the transactions that comprise the recapitalization, which are discussed below.

The recapitalization includes a commitment by Kestrel and its affiliates to purchase \$16.875 million of new equity capital at a price of \$2.50 per common unit. M2 has agreed to provide a standby commitment to purchase an additional number of common units equal to the number of common units not purchased in the rights offering at a purchase price of \$2.25 per unit. We would utilize the \$56.25 million in new equity financing (less expenses of approximately \$6.5 million), together with additional funds from operations, to repurchase at least \$60 million in face amount of our senior notes and, at our option, up to approximately \$73.1 million of senior notes (less any principal, interest and premium payments required to be reserved for non-tendering noteholders in the senior notes tender offer). In addition, certain noteholders have agreed to convert approximately \$26.9 million in face amount of such senior notes into 13,433,962 (subject to adjustment based on rounding) new common units at a conversion price of \$2.00 per unit in connection with the closing of the recapitalization.



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*Unit Purchase Agreement.* We have entered into the unit purchase agreement with Kestrel and its affiliates, which provides for, among other things: the receipt by us of \$56.25 million in new equity financing through the issuance to Kestrel's affiliates of 6,750,000 common units at \$2.50 per unit for an aggregate of \$16.875 million and the issuance of an additional 19,687,500 common units in the rights offering to our common unitholders at an exercise price of \$2.00 per unit for an aggregate of \$39.375 million, which amount will increase in the event our common unitholders do not fully subscribe in the rights offering. The rights will be non-transferable, and an affiliate of Kestrel has agreed to buy any common units not subscribed for in the rights offering at a purchase price of \$2.25 per unit or a total of \$44.3 million. Under the terms of the unit purchase agreement, which has been approved by our unitholders, Kestrel Heat will become our new general partner and Star Gas, our current general partner, will receive no consideration for its withdrawal as general partner.

*Noteholder Agreements.* We have entered into agreements with an unaffiliated group of investors who hold approximately 94% of the principal amount of our senior notes (sometimes referred to in this prospectus as the consenting noteholders) that provide that these noteholders will tender their senior notes to us at par for:

a pro rata portion of \$60 million or, at our option, up to approximately \$73.1 million in cash (less any principal, interest and premium payments required to be reserved for non-tendering noteholders in the senior notes tender offer);

13,433,962 (subject to adjustment based on rounding) new common units at a conversion price of \$2.00 per unit (which new units would be acquired by certain noteholders exchanging approximately \$26.9 million in face amount of senior notes); and

new notes representing the remaining face amount of the tendered notes.

Effective March 23, 2006, we entered into a subsequent agreement with certain holders of approximately 3.6% of the principal amount of our senior notes (also consenting noteholders). The closing of the tender offer for 98% of the senior notes is conditioned upon the simultaneous closing of the transactions under the Kestrel unit purchase agreement.

The closing of the recapitalization will be deemed a change of control under the indenture for our senior notes. Consequently, we will be required to make an offer to repurchase any senior notes that are not otherwise tendered in the senior notes tender offer at a purchase price equal to 101% of their face value. As of the date of this prospectus, the holders of an aggregate of approximately \$5.8 million in senior notes have not yet agreed to tender their notes in the tender offer. The principal amount of any senior notes, plus any interest and premium payments that we are required to make in respect of senior notes tendered for repurchase in the change of control repurchase offer, will reduce on a dollar-for-dollar basis the amount of senior notes that we shall repurchase for cash in connection with the closing of the recapitalization.

Subject to and until the closing of the recapitalization, these noteholders have agreed not to accelerate indebtedness due under the senior notes or initiate any litigation or proceeding with respect to the senior notes. The consenting noteholders have further agreed:

to waive certain potential defaults under the indenture;

not to tender their senior notes in the change of control offer which will be required to be made by us following the closing of the transactions under the unit purchase agreement with Kestrel; and

to consent to certain amendments to the existing indenture.

The agreements with the consenting noteholders further provide for the termination of their provisions in the event that the Kestrel unit purchase agreement is no longer in effect. The understandings and agreements contemplated by these transactions will terminate if the recapitalization does not close prior to April 30, 2006.

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*Amendments to Partnership Agreement.* The unit purchase agreement provides for the adoption of a second amended and restated agreement of limited partnership that will, among other things, provide for the following:

*Conversion of Senior Subordinated Units and Junior Subordinated Units into Common Units.* The proposed amendments will provide for the mandatory conversion of each outstanding senior subordinated unit and each junior subordinated unit into one common unit, as a result of which the subordination period (as defined in our partnership agreement) will end.

*Reduction of the Minimum Quarterly Distribution.* The proposed amendments will reduce the minimum quarterly distribution on the common units from \$0.575 per unit per quarter, or \$2.30 per unit per year, to \$0.0 per unit through September 30, 2008, or, if we elect to commence making distributions sooner, the quarter in which any distribution of available cash is made, and to \$0.0675 per unit per quarter, or \$0.27 per unit per year, thereafter. The amendment will also eliminate all previously accrued cumulative distribution arrearages of \$3.45 per common unit, which aggregated \$111.0 million at February 14, 2006. We believe that this amendment will more closely align the minimum quarterly distribution with the levels of available cash that we may be expected to generate in the future.

*Reduction of Incentive Distribution Levels.* The proposed amendments will reduce the target distribution levels for the incentive distribution rights so that, commencing with the quarter beginning October 1, 2008, or, if we elect to commence making distributions sooner, the quarter in which any distribution of available cash is made, the new general partner units in the aggregate will be entitled to receive 10% of the cash distributions in a quarter once each common unit and general partner unit has received \$.0675 for that quarter, plus any arrearages on the common units from prior quarters, and 20% of the cash distributions in a quarter once each common unit and general partner unit has received \$.1125 for that quarter, plus any arrearages on the common units from prior quarters. Under the partnership agreement as currently in effect, the senior subordinated units, junior subordinated units and general partner units are not entitled to receive incentive distributions until \$0.604 has been distributed on each common unit for a quarter, plus any arrearages on the common units for prior quarters.

*Suspension of Mandatory Distribution of Available Cash.* We suspended distributions on our senior subordinated units, junior subordinated units and general partner units on July 29, 2004 and on our common units on October 18, 2004. The proposed amendments will provide that we are not required to distribute available cash through the quarter ending September 30, 2008. We currently do not intend to make distributions of available cash during this period, even if we have available cash to distribute.

*Reasons for the Recapitalization*

During fiscal 2004, we experienced difficult operating and financial conditions as a result of our inability to pass on the full impact of record wholesale heating oil prices to customers and the effects of unusually high net customer attrition principally related to our heating oil segment's operational restructuring. Prior to the 2004 winter heating season, our heating oil segment attempted to develop a competitive advantage in customer service, and as part of that effort, centralized its heating equipment service dispatch and engaged a centralized call center to fulfill its telephone requirements for the majority of its home heating oil customers. We experienced difficulties in advancing this initiative during the fiscal year ended September 30, 2004, which adversely impacted our customer base, product sales and costs. These conditions led to the suspension of distributions on our senior subordinated units, junior subordinated units and general partner units on July 29, 2004 and to the suspension of distributions on the common units on October 18, 2004. We continued to experience difficult operating and financial conditions in fiscal 2005. As indicated below, we believe that the recapitalization would permit us to address the problems resulting from these difficult operating and financial conditions in a manner that would be beneficial to our unitholders.

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### *Certain Potential Advantages of the Proposed Recapitalization to Common Unitholders:*

*Reduce Liquidity Concerns.* The use of the \$56.25 million in new equity financing (including from this rights offering) (less estimated expenses of \$6.5 million), together with additional funds from operations, to repurchase up to approximately \$73.1 million in face amount of our senior notes (assuming full noteholder participation in the senior notes tender offer), and the conversion of an additional \$26.9 million in face amount of senior notes into equity in connection with the closing of the recapitalization would substantially strengthen our balance sheet and thereby reduce our concerns about liquidity and a shortage of capital. We believe this would provide us with the financial flexibility to better manage this period of high oil prices and to continue our program to improve operating results. As of the date of this prospectus, the holders of an aggregate of approximately \$5.8 million in senior notes have not yet agreed to tender their notes in the tender offer. The principal amount of any senior notes, plus any interest and premium payments that we are required to make in respect of senior notes tendered for repurchase in the change of control repurchase offer, will reduce on a dollar-for-dollar basis the amount of senior notes that we shall repurchase for cash in connection with the closing of the recapitalization.

*Facilitate Future Acquisitions.* The repayment or conversion into equity of senior notes pursuant to the senior notes tender offer would significantly reduce our indebtedness, which should help to facilitate our access to the capital markets to obtain equity capital and debt financing for acquisitions. If we are unable to access additional capital to grow our business, we may be adversely affected in our ability to maintain or increase our customer base, which could further erode our ability to generate available cash. Reducing our indebtedness should enhance our ability to make acquisitions.

*Simplify Capital Structure.* The elimination of the cumulative common unit arrearages and the conversion of the senior subordinated units and junior subordinated units into common units would simplify our capital structure, which should help to facilitate our access to the capital markets. We believe that it would be difficult to issue new common or subordinated units while our existing common units are subject to significant arrearages for past distributions, which could adversely affect our ability to obtain debt financing for acquisitions since an important element of obtaining debt financing is our ability to access equity markets to repay debt. If we are limited in our ability to access capital to grow the business, we may be adversely affected in our ability to maintain or increase our customer base. Such reduction of activity could further erode our ability to generate available cash.

*Experience of Kestrel Representatives.* Subject to the closing of the transactions contemplated by the unit purchase agreement, Star Gas will withdraw as general partner and Kestrel Heat will become our new general partner. Kestrel will be entitled to elect the board of directors of the general partner. We expect to benefit from the ability of the Kestrel representatives who have substantial experience in the energy markets. Paul A. Vermynen, Jr., the President of Kestrel, served as an executive officer of Meenan Oil Co., L.P., a heating oil company, for 18 years before it was sold to Star Gas Partners in 2001. See Information Regarding Kestrel Heat.

*Agreements with Senior Noteholders.* The agreements with the holders of approximately 98% of our senior notes would largely eliminate the costs and significant risks associated with the potential for litigation and alleged defaults under the indenture for our senior notes involving, among other matters, our use of proceeds from the sale of our propane segment. If this matter were not resolved and we were unsuccessful in defending our position in any future claim that might be brought by noteholders, this would constitute an event of default if declared by either of the holders of 25% in principal amount of the senior notes or by the trustee and in such event all amounts due under the senior notes would become immediately due and payable. An acceleration of our senior notes would have a material adverse effect on our ability to continue as a going concern. The report of our independent registered public accounting firm on our consolidated financial statements as of September 30, 2005 and 2004, and for the three years ended September 30, 2005, includes an explanatory paragraph with respect to the impact of this matter on our ability to continue as a going concern if this matter is resolved adversely to us.



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*Certain potential disadvantages of the proposed recapitalization to common unitholders:*

*Elimination of Previously Accrued Cumulative Distribution Arrearages.* Arrearages on the common units that have accrued through the date of the closing of the recapitalization proposal would be eliminated. As of February 14, 2006, cumulative distribution arrearages on all outstanding common units aggregated \$111.0 million, or \$3.45 per common unit.

*Reduction and Postponement of Minimum Quarterly Distributions.* The consummation of the recapitalization would result in a reduction of the minimum quarterly distribution from the current \$0.575 per common unit to \$0.0675 per common unit. Also there would be no mandatory distributions on the common units until at least fiscal 2009. However, regardless of whether the minimum quarterly distribution is reduced, our board of directors of our general partner has concluded that (absent the proposed recapitalization) we are not generating enough available cash to pay any quarterly distributions and/or arrearages at the present time or in the foreseeable future.

*Increased Distributions to General Partner.* Under the proposals which were approved by our unitholders, the general partner will be entitled to receive a substantially higher percentage of cash distributed above \$0.0675 per unit than under the existing partnership agreement as a result of the revisions to the incentive distribution payments to allocate all incentive distributions to the holders of the general partner units. The reduction of the minimum quarterly distribution would mean that the general partner would be able to receive incentive distributions sooner. See Amendments to the Partnership Agreement Comparison of the Star Gas Partnership Agreement Before and After the Recapitalization.

*Depressed Purchase Price.* The price per common unit that we would receive from Kestrel Heat and M2 and in connection with the rights offering is close to the bottom of the trading range for our common units since we became a public partnership, but such price represents a 34% premium to the closing sales price of the common units on the last trading day prior to the public announcement of the recapitalization transaction.

*Substantial Dilution.* The number of common units outstanding would increase from 32,165,528 to approximately 75,774,336, representing a significant dilution to existing unitholders. However, common unitholders who participate in the rights offering would be able to reduce the dilution in their unit holdings. Prior to the recapitalization, the common units represented approximately 88.8% of the total number of units outstanding. Following the recapitalization, if all rightsholders exercise their rights in this rights offering, our existing common unitholders would own common units representing approximately 68.1% of the total number of units outstanding. However, if none of the rightsholders exercise their rights in this rights offering and M2 is issued the 19,687,500 common units offered to the rightsholders hereunder pursuant to its standby commitment, our existing common unitholders would own common units representing approximately 42.3% of the total number of units outstanding.

*Termination of Subordination Period.* The termination of the subordination period would eliminate the priority of payment to the common unitholders in preference to the senior subordinated units and junior subordinated units. In addition, the termination of the subordination period would eliminate the requirement that the general partner receive unitholder approval for issuance of more than a specified number of additional common units during the subordination period. However, the rules of the NYSE generally would require prior unitholder approval before we could issue common units in excess of 20% of the then currently issued and outstanding common units in a single or series of related transactions other than a public offering for cash.

*Restriction on Use of NOLs.* We believe that the issuance of units in our recapitalization will likely result in an ownership change of our corporate subsidiary, Star/Petro, Inc. ( Star/Petro ) under the Internal Revenue Code of 1986, as amended ( Tax Code ). As a result of this ownership change, Star/Petro will be materially



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restricted in its ability to use its net operating loss carryforwards to reduce its future taxable income. As of December 31, 2005, Star/Petro had a federal net operating loss carryforward of approximately \$166.4 million. The net operating loss carryforwards (prior to an ownership change ) will begin to expire in 2025 and are generally available to reduce future taxable income that would otherwise be subject to federal income taxes. As a result of the ownership change, Star/Petro will be restricted annually in its ability to use its net operating loss carryforwards to reduce its federal taxable income. We believe that the restriction may entirely eliminate Star/Petro's ability to use its net operating loss carryforwards. The restriction on Star/Petro's ability to use net operating loss carryforwards to reduce its federal tax liability will reduce the amount of cash Star/Petro has available to make distributions to us. Consequently, the restriction will reduce the amount of cash we have available to distribute to our unitholders.

## **Soros Proposal**

*Original Soros Group Proposal.* On February 15, 2006, a consortium (the Soros Group ) consisting of Soros Fund Management, LLC ( Soros ), Atticus Capital LP ( Atticus ) and Almeida Oil Co., Inc. ( Almeida ) submitted an unsolicited proposal for the recapitalization of Star Gas Partners (the original Soros Group proposal ). The original Soros Group proposal contemplated a similar structure to the recapitalization which Star Gas Partners entered into on December 5, 2005 with Kestrel, except the original Soros Group proposal contemplated that the rights offering to common unitholders would be made at \$2.60 instead of \$2.00 per unit and that Soros Group's equity investment would also be made at \$2.60 per unit instead of \$2.00 per unit as provided under the original Kestrel transaction. The original Soros Group proposal would have provided Star Gas Partners with an additional \$15 million of equity capital for Star before considering certain termination fee, expense reimbursement, incremental transaction expenses and interest costs which are estimated to aggregate approximately \$9.5 million, resulting in additional available cash of approximately \$5.5 million.

The Board of Directors of Star Gas met later in the day on February 15, 2006 with Star Gas Partners' legal and financial advisors to discuss the original Soros Group proposal. At this meeting, Star Gas Partners' legal advisors reviewed with the Board the provisions of the Kestrel unit purchase agreement that govern the manner in which Star Gas Partners may respond to a competing recapitalization proposal. After discussion, the Board requested that Star Gas Partners' legal advisors seek written clarification from the Soros Group concerning the terms of its proposal in order to permit the Board to determine whether the original Soros Group proposal constituted a superior proposal to the Kestrel transaction in accordance with the requirements of the Kestrel unit purchase agreement. The Board also requested that Jefferies & Company, Inc. ( Jefferies ), Star Gas Partners' financial advisor, evaluate the original Soros Group proposal in order to assist the Board in the Board's determination as to whether the Soros Group proposal may reasonably be expected to be more favorable to Star Gas Partners or its unitholders or partners from a financial point of view than the Kestrel transaction.

On February 16, 2006, Star Gas Partners issued a press release with respect to the receipt of the original Soros Group proposal.

In addition, on February 16, 2006, counsel for Star Gas Partners sent a letter to counsel to the Soros Group seeking clarification of certain terms of the original Soros Group proposal. Counsel to the Soros Group responded to this letter on February 17, 2006, and confirmed certain aspects of the original Soros Group proposal, including, among other things, that the senior subordinated units and junior subordinated units would be converted into common units on a one-for-one basis, Star Gas Partners (rather than the Soros Group) would pay any termination fee and expense reimbursement due under the Kestrel unit purchase agreement and that certain of the ancillary agreements, such as the amended and restated partnership agreement and the form of indentures, would be the same under the Soros Group proposal as under the Kestrel transaction. Counsel to Star Gas Partners sent a follow-up letter to counsel to the Soros Group on February 20, 2006 seeking additional

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information concerning the original Soros Group proposal and Almeida's role in the transaction. Counsel to the Soros Group responded to this request on February 21, 2006.

The Board of Directors of Star Gas met on February 23, 2006 to review the original Soros Group proposal. At this meeting, the Board received a presentation from Jefferies comparing the financial terms and other aspects of the original Soros Group proposal and the Kestrel transaction.

After carefully reviewing and considering the financial terms, timing considerations, market risks and potential benefits and detriments of the original Soros Group proposal, and after consulting with its financial advisors and outside legal counsel, the Board of Directors of Star Gas (with Mr. Sevin abstaining) concluded that the original Soros Group proposal was not a superior proposal under the terms of the original Kestrel unit purchase agreement.

The original Soros Group proposal was determined not to be superior for a number of reasons. First, under the Soros Group proposal, existing common unitholders would pay \$2.60 per unit to purchase additional units offered in the rights offering. However, under the original Kestrel transaction, existing common unitholders would pay \$2.00 to participate. Because the dollar amount being raised in the rights offering is the same in both proposals, this means that, under the original Soros Group proposal, existing common unitholders are afforded rights to purchase approximately 0.42 units for each existing common unit while the original Kestrel transaction provides the right to purchase approximately 0.54 units for each existing common unit. As a result, existing common unitholders' ownership would be diluted to approximately 61.4% of the outstanding common units under the original Soros Group proposal compared to approximately 66.8% of the outstanding common units under the original Kestrel transaction, in each case assuming the rights offering is fully subscribed by common unitholders. Second, while the Board recognized that the original Soros Group proposal would provide additional equity capital to Star Gas Partners, after deducting the \$4 million termination fee and \$0.5 million expense reimbursement due under the Kestrel agreement (which would be required to be paid by Star Gas Partners) and the estimated \$3.3 million in incremental transaction expenses and \$1.7 million in interest that would accrue on the senior notes during an assumed two month period of delay which otherwise would have been repaid or converted to common units, the amount of additional capital provided to Star would only be approximately \$5.5 million.

In comparing the two alternative transactions, the Board concluded, based upon the factors discussed above and the analyses performed by Star Gas Partners' financial advisor, that, from a financial point of view, the two proposals were in many respects substantially equivalent. While certain of the financial analyses indicated the original Soros Group proposal was very slightly accretive on a pro forma basis per unit as compared to the original Kestrel transaction, the additional ownership dilution to existing common unitholders outweighed any such marginal benefit. The original Soros Group proposal also assumed that the existing transactions with Star Gas Partners' senior note holders would remain the same and would be an integral part of the transactions contemplated by the original Soros Group proposal. However, the lockup agreements with the senior noteholders terminate upon the termination of the Kestrel unit purchase agreement, and the original Soros Group proposal provided no assurances that similar lockup agreements would be entered into with Star Gas Partners' senior noteholders and that Star would be able to resolve the pending dispute with its noteholders in a manner similar to the resolution provided in the existing agreements with the noteholders. The Board also noted that the original Soros Group proposal would require Star Gas Partners to obtain a new consent from Star Gas Partners' existing secured lenders under its credit facility, since on February 3, 2006, Star Gas Partners obtained such a consent in connection with the Kestrel unit purchase agreement.

The Board also considered the impact on Star Gas Partners' business and employees in light of the additional uncertainty about the original Soros Group proposal, the time required to consummate a transaction with the Soros Group, and the related additional uncertainty associated with the due diligence review required to

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be undertaken by the Soros Group, and concluded that these factors could pose additional risks to Star Gas Partners under the original Soros Group proposal. The Board also was concerned about potential conflicts of interest and potential antitrust issues under the Clayton Act presented by the original Soros Group proposal which contemplates having Robert Almeida, who is affiliated with a competitor of Star Gas Partners, become one of the directors of the board of the new general partner of Star Gas Partners. The Board was also aware of the fact that if the original Soros Group proposal was determined to be a superior proposal under the Kestrel unit purchase agreement and subsequently such unit purchase agreement was terminated for any reason (including the failure to obtain approval of unitholders at the special meeting), other than a breach by Kestrel, Star Gas Partners would owe Kestrel the termination fee and expense reimbursement.

The Board of Directors of Star Gas weighed the relative timing, certainty and financial aspects of the two proposals and concluded that the incremental cash to Star Gas Partners of the original Soros Group proposal was outweighed by the dilution to existing common unitholders, incremental expenses, timing, uncertainty, antitrust, conflicts and employee-related issues associated with such proposal, and accordingly, the Board concluded that the original Soros Group proposal was not a superior proposal.

During the course of the February 23, 2006 Board meeting, Joseph Cavanaugh, Star Gas Partners chief executive officer, advised the Board that he would be reluctant to continue in such role if the original Soros Group proposal were consummated.

On February 24, 2006, Star Gas Partners issued a press release announcing the Board's determination with respect to the original Soros Group proposal.

*Revised Soros Group Proposal.* On March 3, 2006, Star Gas Partners received a revised recapitalization proposal (the revised Soros Group proposal) from the Soros Group which includes, among other things, a proposed commitment by the Soros Group of \$32.5 million of new equity capital (compared to their prior proposal of \$30 million) in which they would purchase 10 million common units at a price of \$3.25 per unit. The revised Soros Group proposal contemplates a standby commitment in a \$37.5 million (compared to the prior proposal of \$35 million) rights offering to Star Gas Partners common unitholders, at a price of \$2.50 (compared to the prior proposal of \$2.60) per common unit. The revised Soros Group proposal would result in the aggregate issuance of 25 million new common units (exclusive of new common units to be issued to noteholders in the notes for units exchange and new common units to be issued to existing holders of Star Gas Partners senior subordinated and junior subordinated units upon the conversion of such units into common units) and cash to Star Gas Partners of \$70 million (compared to the prior proposal of \$65 million) prior to the payment of fees, expenses and other costs. Pursuant to the Soros Group proposal, the Soros Group would become the new general partner of Star Gas Partners.

The revised Soros Group proposal contemplates maintaining the current arrangements with the holders of approximately 98% in principal amount of Star Gas Partners senior notes, including the conversion of \$26.9 million of senior notes into common units at \$2.00 per common unit. The revised Soros Group proposal also indicated that while it is not conditioned on any change to the arrangements with Star Gas Partners senior noteholders, the Soros Group would be prepared to explore a revised arrangement between Star Gas Partners and its noteholders, which would include a bridge financing facility, provided by the Soros Group, to permit Star Gas Partners to make an asset sales proceeds offer to the senior noteholders under the terms of their indenture. The revised Soros Group proposal, like the original proposal, is subject to completion of a confirmatory due diligence review and negotiation and execution of definitive agreements.

On March 6, 2006, counsel for Star Gas Partners sent a letter to counsel to the Soros Group seeking clarification of certain terms of the revised Soros Group proposal, including the terms and amount of the bridge financing facility. Counsel to the Soros Group responded to this letter on March 7, 2006 and declined to provide



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the information requested by our counsel until such time as Star Gas Partners confirmed that it was ready to discuss the revised Soros Group proposal with the Soros Group.

On March 6, 2006, Star Gas Partners issued a press release announcing the Board's receipt of the revised Soros Group proposal.

The Board of Directors of Star Gas met on March 6, 2006 with Star Gas Partners' legal and financial advisors to discuss the revised Soros Group proposal. After discussion, the Board requested that Jefferies evaluate the revised Soros Group proposal in order to assist the Board in the Board's determination as to whether the revised Soros Group proposal may reasonably be expected to be more favorable to Star Gas Partners or its unitholders or partners from a financial point of view than the original Kestrel transaction.

*Kestrel Proposal and Revised Kestrel Proposal.* On March 8, 2006, Star Gas Partners received a proposal from Kestrel to amend the existing unit purchase agreement (the Kestrel proposal) as well as a subsequent revised proposal from Kestrel (the revised Kestrel proposal).

The Kestrel proposal included, among other things, an increased commitment by Kestrel to \$19.5 million of new equity capital (increased from the original unit purchase agreement which provided for a \$15 million equity investment) in which they would purchase 7.5 million common units at a price of \$2.60 per unit. The Kestrel proposal also contemplated increasing to \$41.125 million the rights offering to Star Gas Partners common unitholders, at a price of \$2.35 per common unit (compared to the terms of the original unit purchase agreement which provided for a \$35 million rights offering at a price of \$2.00 per common unit), which Kestrel would continue to backstop. The Kestrel proposal would result in the same aggregate issuance of 25 million new common units (exclusive of new common units to be issued to noteholders in the notes for units exchange and new common units to be issued to existing holders of Star Gas Partners' senior subordinated and junior subordinated units upon the conversion of such units into common units) as under the existing Kestrel transaction and cash to Star Gas Partners of \$60.625 million (compared to the original commitment by Kestrel of \$50 million) prior to the payment of other costs.

The Kestrel proposal was conditioned on the elimination of the fiduciary out provisions set forth in Section 5.11 of the Kestrel unit purchase agreement, which provisions, among other things, allow the Board to consider and approve proposals by third parties which may increase the value to Star Gas Partners and its unitholders.

The Kestrel proposal indicated that, other than the terms set forth above, the terms and provisions of the original unit purchase agreement with Kestrel would remain in full force and effect.

The Kestrel proposal also indicated that it would, by its terms, expire and be of no further force and effect, if not previously accepted by Star Gas Partners, at the earlier of (i) 4:00 p.m. Eastern Time on March 9, 2006 or (ii) such time as Star Gas Partners makes a public announcement with respect to its determination of whether the previously announced revised Soros Group proposal constitutes a superior proposal under the terms of the Kestrel unit purchase agreement.

The Board of Directors of Star Gas met on March 8, 2006 to review the revised Soros Group proposal and the Kestrel proposal. At this meeting, the Board received a presentation from Jefferies comparing the financial terms and other aspects of the revised Soros Group proposal and the original Kestrel transaction. The Board also requested that Jefferies evaluate the Kestrel proposal in order to assist the Board in the Board's determination as to whether the revised Soros Group proposal was more favorable from a financial point of view than the Kestrel proposal.

It was the sense of the Board that while no final decision would be made regarding the Kestrel proposal until the Board had the opportunity to review Jefferies' further analysis, it was not inclined, under current



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circumstances, to accept a proposal that would prematurely eliminate the fiduciary out provision of its existing agreement with Kestrel, which would effectively foreclose the Board's ability to entertain superior proposals and engage in discussions to secure additional value for Star Gas Partners and its unitholders.

The Board requested that Star Gas Partners' legal advisors contact Kestrel to determine if Kestrel would be willing to eliminate the fiduciary out provision of its revised proposal.

In response to the Board's concerns regarding the elimination of the fiduciary out provision in the Kestrel proposal, Kestrel subsequently advised Star Gas Partners that if the Board rejected the Kestrel proposal, Kestrel would make a revised proposal (the revised Kestrel proposal), which would provide for an increase in Kestrel's equity investment to \$16.875 million of new equity capital in which they would purchase 7.5 million common units at a price of \$2.25 per common unit, and an increased \$39.375 million rights offering to Star Gas Partners' holders of common units at a price of \$2.25 per common unit. The revised Kestrel proposal would result in the same aggregate issuance of 25 million new common units (exclusive of new common units to be issued to noteholders in the notes for units exchange and new common units to be issued to existing holders of Star Gas Partners' senior subordinated and junior subordinated units upon the conversion of such units into common units) as under the original Kestrel transaction and cash to Star Gas Partners of \$56.25 million prior to the payment of certain costs and expenses.

On March 9, 2006, Star Gas Partners issued a press release announcing the Board's receipt of the Kestrel proposal and the revised Kestrel proposal.

The Board of Directors of Star Gas met on March 9, 2006 with Star Gas Partners' legal and financial advisors to discuss the Kestrel proposal and the revised Kestrel proposal. After discussion, the Board rejected the Kestrel proposal. The Board did not believe that the Kestrel proposal was sufficiently attractive to justify accepting a proposal which would eliminate the fiduciary out provision of its existing agreement with Kestrel, which could adversely affect the Board's ability to secure additional value for Star Gas Partners and its unitholders. The Board then approved the revised Kestrel proposal and authorized management to enter into an amendment to the unit purchase agreement to implement the revised Kestrel proposal. The Board requested that Jefferies evaluate the revised Kestrel proposal against the revised Soros Group proposal in order to assist the Board in the Board's determination as to whether the revised Soros Group proposal may reasonably be expected to be more favorable to Star Gas Partners or its unitholders or partners from a financial point of view than the revised Kestrel proposal.

At the March 9, 2006 Board meeting, the Board also approved a postponement of the date of the special meeting of unitholders until March 24, 2006, in order to give Star Gas Partners time to prepare and circulate additional information to unitholders. The Board also set the record date for the rights offering as of the close of business on March 28, 2006 (which the Board later reset to April 6, 2006). On March 9, 2006, Star Gas Partners issued a press release announcing the Board's approval of the revised Kestrel proposal.

On March 9, 2006, Star Gas Partners entered into a letter agreement with Kestrel which contemplated an amendment to the Kestrel unit purchase agreement. The contingent amendment, which reflects the terms of that letter agreement, provides for an increased equity investment by Kestrel of \$16.875 million at a price of \$2.25 per common unit and an increased rights offering of \$39.375 million to Star's common unitholders at a price of \$2.25 per common unit. The contingent amendment would result in the aggregate issuance of 25 million new common units (exclusive of new common units to be issued to noteholders in the notes for units exchange and new common units issued to existing holders of Star's senior subordinated and junior subordinated units) and cash to Star Gas Partners of \$56.25 million.

The contingent amendment provided that it would only become effective, and amend the existing unit purchase agreement, upon the satisfaction of either of the following conditions: (1) if Star Gas Partners received



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the consent to the contingent amendment from holders of the holders of 2/3 of Star Gas Partners' outstanding senior notes prior to the close of business on Tuesday, March 28, 2006; or (2) if Kestrel and Star Gas Partners mutually agreed in writing to such effectiveness.

Subsequent to executing the letter agreement, Star Gas Partners was advised that two of its senior noteholders (the non-consenting noteholders) were withholding their consent to amending the Kestrel agreement, effectively prohibiting Star Gas Partners from obtaining the increased value for all stakeholders provided by the revised Kestrel proposal.

The Board met on March 10, 2006 to continue its review of the revised Soros Group proposal. At this meeting, the Board received a presentation from Jefferies comparing the financial terms and other aspects of the revised Soros Group proposal and the revised Kestrel proposal.

The Board met on March 12, 2006 to continue its review of the revised Soros Group proposal and the revised Kestrel proposal. At this meeting, the Board authorized management to enter into the contingent amendment, which was executed later that day.

On March 13, 2006, the Partnership issued a press release concerning, among other things, the signing of the contingent amendment and the position being taken by the non-consenting noteholders.

The Board met with its legal and financial advisors on March 14, 2006 to continue to discuss developments related to the non-consenting noteholders.

On March 15, 2006, the non-consenting noteholders sold their notes to other noteholders who were in favor of, and consented to, the contingent amendment. The contingent amendment, by its terms, became effective upon the receipt by Star Gas Partners of consents from the holders of more than 2/3 of Star Gas Partners' outstanding senior notes.

The Board met on March 15, 2006 to continue its review of the revised Soros Group proposal. After carefully reviewing and considering the transaction risks, financial terms, timing considerations, market risks and potential benefits and detriments of the Kestrel unit purchase agreement, as amended by the contingent amendment, and the revised Soros Group proposal, and after consulting with its financial advisors and outside legal counsel, which included reviewing and considering the presentation that Jefferies made at the March 10, 2006 meeting of the Board of Directors, the Board (with Mr. Sevin abstaining) concluded that the revised Soros Group proposal was not a superior proposal under the terms of the Kestrel unit purchase agreement, as amended by the contingent amendment (the amended unit purchase agreement).

The revised Soros Group proposal was determined not to be a superior proposal for a number of reasons. The revised Soros Group proposal, like the original Soros Group proposal, has failed to provide any assurances of entering into acceptable lockup agreements with Star Gas Partners' senior noteholders. The revised Soros Group proposal mentioned the possibility of providing a bridge financing facility to avoid the risks associated with Star Gas Partners' senior noteholders; however, when asked for additional information, the Soros Group declined to provide any details as to the terms or amount of its supposed bridge financing facility. The revised Soros Group proposal continued to assume that the existing transactions with Star Gas Partners' senior noteholders would remain the same and would be an integral part of the transactions contemplated by the revised Soros Group proposal. The lockup agreements with the senior noteholders would terminate upon the termination of the Kestrel agreement, and the revised Soros Group proposal provided no assurances that similar lockup agreements would be entered into with Star Gas Partners' senior noteholders or that Star Gas Partners would be able to similarly resolve the dispute with its noteholders regarding the use of proceeds from the sale of its



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propane business or that Star Gas Partners would be able to deleverage its senior notes by up to \$100 million (as is provided for in the Kestrel transaction).

After consulting with its financial advisor, the Board concluded that the amended unit purchase agreement provided Star Gas Partners terms which were slightly better from a financial point of view than the revised Soros Group proposal. Under the revised Soros Group proposal the existing common unitholders must pay \$2.50 per unit to purchase additional units offered in the rights offering compared to the amended unit purchase agreement, which only requires existing common unitholders to pay \$2.25 to participate. Factoring in the discrepancy in the number of units proposed to be offered pursuant to the amended unit purchase agreement and revised Soros rights offerings respectively, the existing common unitholders are afforded rights to purchase approximately 0.466 units for each existing common unit in the revised Soros Group proposal compared to approximately 0.544 units for each existing common unit under the amended unit purchase agreement. As a result, the existing common unitholders' ownership would be diluted to approximately 63.4% under the revised Soros Group proposal compared to only approximately 66.8% dilution under the amended unit purchase agreement (assuming in all instances that the rights offerings would both be fully subscribed). Under various analyses relating to the use of the incremental cash in the two proposals (i.e., investing cash, reducing debt, repurchasing units or making accretive acquisitions), the Kestrel transaction yielded slightly greater potential long-term value to the existing common unitholders in all cases assuming in all instances that the rights offering in each of the revised Soros Group proposal and Kestrel transaction are fully subscribed. The Board also had some concern about the potential adverse income tax consequences to Star Gas Partners unitholders who participate in the rights offering paying \$2.50 per common unit while the Soros Group paid a higher price of \$3.25 per common unit for the same Partnership interests.

While the Board recognized that the revised Soros Group proposal would provide additional cash to Star Gas Partners, after deducting the termination fee and expense reimbursement due under the amended unit purchase agreement and the estimated incremental transaction expenses and interest that would accrue during any period of delay on the senior notes which otherwise would have been repaid or converted to common units, the amount of additional cash provided to Star Gas Partners would be approximately \$4.25 million.

The Board also considered the impact on Star Gas Partners' business and employees in light of the additional uncertainty about the Soros Group's proposal, the time required to consummate a transaction with the Soros Group, and the related additional uncertainty associated with the due diligence review required to be undertaken by the Soros Group, and the additional effort and expense required to obtain a new vote of common and subordinated unitholders for the revised Soros Group proposal, and concluded that these factors could pose additional risks to Star Gas Partners under the revised Soros Group proposal.

In comparing the revised Soros Group proposal to the amended unit purchase agreement, the Board concluded, based on the factors discussed above and the analyses performed by its financial advisor, the Kestrel transaction was slightly better, from a financial point of view, than the revised Soros Group proposal.

After weighing the relative timing, certainty and financial aspects of the revised Soros Group proposal as compared to the Kestrel transaction and its associated risks, the Board concluded that the incremental cash to Star Gas Partners of the revised Soros Group proposal was outweighed by the risk and uncertainty associated with the revised Soros Group proposal, the dilution to existing unitholders, expenses, timing, employee-related issues and the heightened uncertainty that the Soros Group would be able to replicate in a timely manner the current arrangements with Star Gas Partners' senior noteholders, and accordingly, the Board could not at this time conclude that the Soros Group's revised proposal was a superior proposal under the terms of the amended unit purchase agreement.

On March 16, 2006, Star Gas Partners issued a press release announcing the effectiveness of the contingent amendment and the Board's determination concerning the revised Soros Group proposal.



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*New Soros Group Proposal.* On March 22, 2006, we received a new unsolicited and non-binding competing proposal (the New Soros Group proposal) from the Soros Group which included, among other things, a proposed tender offer by the Soros Group for up to 15 million common units at a price of \$3.00 per unit. The New Soros Group proposal contemplated a \$67.5 million rights offering to Star Gas Partners' common unitholders at a price of \$2.25 per common unit, with the common units purchased by the Soros Group through the tender offer being eligible to participate in the rights offering and the Soros Group providing a standby commitment to backstop the entire rights offering. The New Soros Group proposal would result in the aggregate issuance of 30 million new common units and cash to Star Gas Partners of \$67.5 million prior to the payment of termination fees, expenses, incremental interest on Star Gas Partners' senior notes and other costs.

The New Soros Group proposal did not include a conversion of the Partnership's senior subordinated and junior subordinated units into Star Gas Partners' common units. The Soros Group did, however, inform the Partnership that the Soros Group proposal could be adjusted to allow for such a conversion if the Board of Star Gas thought such a conversion was necessary or desirable.

Pursuant to the New Soros Group proposal, Star Gas would remain the general partner of Star Gas Partners, and the Soros Group would have the right to appoint all of the directors of the general partner. The New Soros Group proposal contemplated that Star Gas would, in consideration of the Soros Group's standby commitment in the rights offering, (a) agree to relinquish its right to receive distributions from Star Gas Partners pursuant to Star Gas Partners' partnership agreement (other than with respect to capital actually invested in Star Gas Partners) and (b) cause Star to issue to the Soros Group newly created units which would provide economic benefits substantially equivalent to the new general partner's rights to receive distributions under the amended unit purchase agreement.

The New Soros Group proposal contained a number of additional conditions not contained in any prior proposal. The proposal was conditioned on the board of Star Gas approving the transactions, including the tender offer, contemplated by the New Soros Group proposal and revoking all anti-takeover protections currently contained in the formation and governance documents of the Partnership and its general partner solely with respect to the New Soros Group proposal. The New Soros Group Proposal was also conditioned upon the transfer, for nominal consideration, of a minority equity interest in Star Gas to the Soros Group and the agreement by all of the equity holders of Star Gas to: (i) grant the Soros Group the right to appoint all of the members of the board of directors of Star Gas and (ii) not sell their equity interests in Star Gas without the prior written consent of the Soros Group. The proposal was further conditioned on the Soros Group being granted the option to acquire all of the equity interests in Star Gas for a price equal to the value of Star Gas' invested capital in Star Gas Partners at the time of exercise of such option.

The New Soros Group proposal did not contemplate maintaining the current arrangements with the holders of Star Gas Partners' senior notes. The New Soros Group proposal contemplated that the existing arrangements with noteholders would terminate upon the termination of the amended unit purchase agreement and that any future negotiations with such noteholders would be the responsibility of the Soros Group. The New Soros Group proposal indicated that in addition to the cash provided by the rights offering and cash on hand at Star Gas Partners, the Soros Group would arrange debt financing to satisfy any redemption of Star Gas Partners' senior notes required pursuant to the excess proceeds clause of Star Gas Partners' indenture with its senior noteholders. The Soros Group also indicated that they had engaged in discussions with financing sources regarding replacing Star Gas Partners' existing senior bank facility and providing a facility to fund any purchases under the excess proceeds clause of Star Gas Partners' indenture.

The New Soros Group proposal, like the prior Soros Group proposals, was subject to completion of a confirmatory due diligence review and negotiation and execution of definitive agreements, which diligence review the Soros Group had indicated it would be able to conduct in one week.

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On March 23, 2006, Star Gas Partners issued a press release announcing the Board's receipt of the New Soros Group proposal.

In addition, on March 23, 2006, counsel for Star Gas Partners sent a letter to counsel to the Soros Group seeking clarification of certain terms of the New Soros Group proposal. Counsel to the Soros Group responded to this letter on March 27, 2006. Counsel to Star Gas Partners sent a follow-up letter to counsel to the Soros Group on March 28, 2006 seeking additional information concerning the New Soros Group proposal, which counsel to the Soros Group responded to on March 29, 2006.

The Board of Directors of Star Gas met on March 23, 2006 with Star Gas Partners' legal and financial advisors to discuss the New Soros Group proposal. The Board requested that Jefferies evaluate the New Soros Group proposal in order to assist the Board in determining whether the New Soros Group proposal may reasonably be expected to be more favorable to Star Gas Partners or its unitholders or partners from a financial point of view than the amended unit purchase agreement, in connection with the Board's determination of whether the New Soros Group proposal constitutes a superior proposal under the amended unit purchase agreement.

At the March 23, 2006 Board meeting, the Board also approved an adjournment of the date of the special meeting of unitholders until April 6, 2006, in order to give Star Gas Partners time to prepare and circulate additional information to unitholders. The Board also reset the record date for the rights offering as the close of business on April 6, 2006.

On March 24, 2006, Star Gas Partners issued a press release announcing the adjournment of the special meeting and the resetting of the rights offering record date.

The Board met on March 26, 2006 to continue its discussions concerning the New Soros Group proposal, but did not reach any decision since counsel to the Partnership had not yet received a response to its letter to counsel to the Soros Group seeking clarifications of certain terms of the New Soros Group proposal. Jefferies advised the Board that without the requested information, Jefferies would not be able to prepare an evaluation of the New Soros Group proposal for the Board.

On March 28, 2006, Star Gas Partners commenced the tender and exchange offer and consent solicitation for senior notes contemplated by the Kestrel transaction, which is set to expire at 12:00 midnight on April 25, 2006. The tender and exchange offer is conditioned upon the continued effectiveness and closing of the Kestrel transaction.

*New Kestrel Proposal.* On March 29, 2006, Star Gas Partners received a new proposal from Kestrel to further amend the amended unit purchase agreement (the New Kestrel proposal). The New Kestrel proposal included, among other things, an increase in the per unit price being paid by Kestrel to \$2.50 and a reduction in the number of common units being purchased by Kestrel to 6,750,000 resulting in reduced dilution to existing unitholders and no change in Kestrel's aggregate equity investment of \$16.875 million. The New Kestrel proposal also contemplated a decrease in the exercise price per unit in the rights offering to Star Gas Partners' common unitholders to \$2.00 per common unit (from \$2.25) and an increase in the number of common units being offered in the rights offering to 19,687,500 (from 17,500,000), with a standby commitment from M2 to purchase all units that are not subscribed for in the rights offering at a purchase price of \$2.25.

The Board of Directors of Star Gas met on March 29, 2006 to continue its review of the New Soros Group proposal and to discuss the New Kestrel proposal. At this meeting, the Board received a presentation from Jefferies comparing the financial terms and other aspects of the New Soros Group proposal and the Kestrel transaction (before giving effect to the New Kestrel proposal). The Board also requested that Jefferies



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evaluate the New Kestrel proposal in order to assist the Board in the Board's determination as to whether the New Soros Group proposal was more favorable from a financial point of view than the New Kestrel proposal.

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The Board met on March 30, 2006 to continue its review of the New Soros Group proposal and New Kestrel proposal. At this meeting, the Board received a presentation from Jefferies comparing the financial terms and other aspects of the New Soros Group proposal and the New Kestrel proposal.

After carefully reviewing and considering the financial terms, timing considerations, market risks and potential benefits and detriments of the New Soros Group proposal and New Kestrel proposal, and after consulting with its financial advisors and outside legal counsel, the Board of Directors of Star Gas approved the New Kestrel proposal and authorized management to enter into an amendment to the amended unit purchase agreement to implement the New Kestrel proposal. On March 30, 2006, Star Gas Partners entered into the second amendment to the Kestrel unit purchase agreement. The Board also concluded that the New Soros Group proposal was not a superior proposal under the terms of the Kestrel transaction as amended by the New Kestrel proposal.

The New Soros Group proposal was determined not to be superior for a number of reasons. While the Soros Group indicated that they were confident that they would be able to secure or provide sufficient financing to alleviate the risks associated with a potential alleged default being asserted by Star Gas Partners senior noteholders after April 30, 2006 (the date upon which Star Gas Partners lockup agreements with Star Gas Partners senior noteholders terminate), the Soros Group did not provide any details of such financing. The Board considered these factors in light of a recent letter received from counsel to certain of Star Gas Partners senior noteholders who have entered into lockup agreements, which indicated that while such noteholders have not determined whether to exercise their rights and remedies under the senior notes indenture, such noteholders reserved the right to do so following the termination of their lockup agreements. In addition, the Board believed that the New Soros Group proposal would likely trigger the change in control provisions under Star Gas Partners senior note indenture, which could result in Star Gas Partners having to offer to repurchase all \$265 million of these senior notes. The Soros Group has not provided any details as to how it would meet that obligation.

The conditions contained in the New Soros Group proposal also were problematic, as a number of the conditions related to the equity interests of Star Gas Partners general partner. Neither the Board nor Star Gas Partners has the ability to compel the equity holders of Star Gas Partners general partner to comply with the conditions set forth in the New Soros Group proposal and accordingly, there could be no assurance that these conditions would be satisfied. These additional conditions were assessed by the Board in determining the ability of the Soros Group to consummate the transaction contemplated by the New Soros Group proposal.

After consulting with its financial advisors, the Board also concluded that from a financial point of view the New Soros Group proposal was substantially equivalent, but not superior, to the Kestrel transaction. While the Board recognized that the New Soros Group proposal would provide additional cash to Star Gas Partners, after deducting the termination fee and expense reimbursement due under the amended unit purchase agreement and the estimated incremental transaction expenses and interest that would accrue during any period of delay on the senior notes which otherwise would have been repaid or converted to common units in the Kestrel transaction, the amount of additional cash provided to Star Gas Partners would only be approximately \$1.75 million. In addition, the New Soros Group proposal did not assure the same amount of deleveraging as would occur under the Kestrel transaction, which contemplates deleveraging in an amount up to \$100 million.

The Board believed that the \$100 million of debt reduction associated with the Kestrel transaction would stabilize Star Gas Partners financial condition, reduce its interest expense and thereby improve its earnings as well as increase its ability to grow its business through acquisitions. In addition, the Kestrel transaction, unlike the New Soros Group proposal, assures Star Gas Partners that it can redeem up to approximately \$73.1 million of senior notes at par without any premium providing for an efficient use of the cash provided by its proposal. The Board also believed that the relatively small incremental amount of cash to Star Gas Partners in the New Soros Group proposal was outweighed by the lack of deleveraging, the lack of a clear proposal to deal with Star Gas

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Partners' senior noteholders within the existing time parameters of the lockup agreements, the conditions pertaining to Star Gas Partners' general partner's equity holders for which there could be no assurance of satisfaction and the other elements of uncertainty and risks of the New Soros Group proposal.

The Board noted that the financial aspects of the Kestrel transaction had been enhanced by increasing the price Kestrel would pay for its investment in Star Gas Partners from \$2.25 per unit to \$2.50 per unit, while at the same time reducing the price to be paid by common unitholders in the rights offering from \$2.25 per unit to \$2.00 per unit. In addition, the Board noted Kestrel's willingness to backstop the rights offering at a price of \$2.25 per unit, which could result in additional cash for Star Gas Partners to the extent that the rights offering was not fully subscribed for by common unitholders.

The Board also considered the impact on Star Gas Partners' business and employees in light of the additional uncertainty about the New Soros Group's proposal, the time required to consummate a transaction with the Soros Group, the related additional uncertainty associated with the due diligence review required to be undertaken by the Soros Group, and the additional effort and expense required to obtain a new vote of common unitholders (and potentially senior subordinated unitholders) for the Soros Group's revised proposal, and concluded that these factors could pose additional risks to Star Gas Partners under the New Soros Group proposal.

In comparing the New Soros Group proposal to the amended unit purchase agreement, the Board concluded, based on the factors discussed above and the analyses performed by its financial advisors, the New Soros Group proposal did not constitute a superior proposal under the terms of the amended unit purchase agreement.

At the special meeting of Star Gas Partners' unitholders on Thursday, April 6, 2006, our unitholders approved each of the proposals submitted to them for approval and we continue to believe that the recapitalization transaction with Kestrel has a high likelihood of closing.

Since the Board has concluded that the Soros Group proposal is not a superior proposal, Star Gas Partners is precluded under the Kestrel agreement from providing confidential information to, or entering into or participating in discussions or negotiations with, the Soros Group at this time. However, the Board retains the ability to consider unsolicited proposals, and determine that such proposals are superior proposals after the date of the special meeting and to terminate the amended unit purchase agreement in order to accept a superior proposal.

## **Structure**

We are a Delaware limited partnership that was formed in October 1995 in connection with our initial public offering.

Our heating oil operations are conducted through Petro Holdings, Inc. (Petro) and its direct and indirect subsidiaries. Petro is a Minnesota corporation that is a wholly owned subsidiary of Star/Petro, Inc., or Star/Petro, which is our 99.99% subsidiary.

Our general partner is Star Gas LLC, a Delaware limited liability company. Star Gas LLC owns an approximate 1% general partner interest in Star Gas Partners, L.P., or Star Gas Partners, and also owns an approximate .01% interest in our subsidiary, Star/Petro.



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Following the closing of the recapitalization, which has been approved by our unitholders, our general partner will be Kestrel Heat, which will own the general partnership interest in us representing an approximately 0.4% interest, and Star Gas LLC will transfer its .01% interest in Star/Petro to us so that Star/Petro will become a wholly-owned subsidiary of ours.

Our common units (SGU) and senior subordinated units (SGH) are traded on the New York Stock Exchange.

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**Summary of the Rights Offering**

You are entitled to receive .6121 rights for every common unit you hold on the record date. You should read the discussion under the heading **Description of Common Units** beginning on page 83 of this prospectus for a more detailed description of the common units.

We summarize the principal terms of the rights offering below. You should read the discussion under the heading **The Rights Offering** beginning on page 55 of this prospectus for a more detailed description of the rights offering.

The Rights Offering	We will issue to our common unitholders of record on April 6, 2006, non-transferable rights entitling the holders to purchase an aggregate of 19,687,500 common units at a subscription price of \$2.00 per unit. Unitholders will receive .6121 of a right for each common unit owned by them. Each full right is exercisable to purchase one common unit. No fractional rights or cash in lieu thereof will be issued or paid by us. Instead, the number of rights issued by us to each common unitholder on the record date will be rounded up to the nearest whole number of rights.
Standby Commitment	M2 has agreed to purchase all of the common units which are subject to unexercised rights after giving effect to the subscription privilege at purchase price of \$2.25 per unit. No rightsholder will have the right to oversubscribe.
Expiration Time	The rights offering expires at 5:00 P.M., New York City time, on April 25, 2006 (the <b>Expiration Time</b> ), unless we extend the rights offering in our sole discretion, in which case the term <b>Expiration Time</b> means the latest date and time to which the rights offering is extended.
Conditions to the Rights Offering	The closing of the rights offering is subject to the simultaneous closing of the recapitalization. Accordingly, we expect to extend the <b>Expiration Time</b> until such closing. Further, we will complete the rights offering only if it would not violate applicable law or any applicable interpretation of the Staff of the SEC and no injunction, order or decree has been issued and no material disruption in the U.S. financial markets has occurred that would prohibit, prevent or materially impair our ability to proceed with the rights offering. See <b>The Rights Offering</b> <b>Conditions to the Rights Offering</b> .
Procedures for Exercising the Rights	Each rightsholder wishing to exercise its rights must complete its rights certificate and mail or otherwise deliver the rights certificate, together with any other required documentation and payment for the subscription price of the units to be purchased in accordance with the rights certificate, to the subscription agent identified below under <b>Subscription Agent</b> at the address set forth in this prospectus. Please do not send your rights certificate, payment or other documentation to us. Specified brokers, dealers, commercial banks, trust companies and other nominees may also make tenders by book-entry transfer. See <b>The Rights Offering</b> <b>Instructions for Completing Your Rights Certificates</b> and <b>Delivery of Subscription Materials and Payment</b> .

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Exercising a Portion of Your Rights	You may subscribe for fewer than all of the common units that you are eligible to purchase pursuant to the subscription privilege represented by your rights certificate; however, once the rights offering expires, you will no longer be entitled to subscribe for common units. No rightsholder will have the right to oversubscribe.
Special Procedures for Beneficial Owners	Each beneficial owner of common units wishing to exercise its rights must instruct its broker, dealer or other nominee to act on its behalf. To indicate your decision with respect to your rights, you should complete and return to your broker, dealer or other nominee the form entitled Beneficial Owners Election Form. You should receive this form from your broker, dealer or other nominee with the other subscription materials. See The Rights Offering Beneficial Owners.
Guaranteed Delivery Procedures	If you wish to exercise your rights, but you do not have sufficient time to deliver the rights certificate evidencing your rights to the subscription agent before the Expiration Time, you may exercise your rights by providing your payment in full of the subscription price for each common unit being subscribed for pursuant to the subscription privilege to the subscription agent before the Expiration Time, delivering a notice of guaranteed delivery to the subscription agent at or before the Expiration Time and delivering the properly completed rights certificate evidencing the rights being exercised (and, if applicable for a nominee holder, the related nominee holder certification), with any required signatures guaranteed, to the subscription agent, within three business days following the date the notice of guaranteed delivery was received by the subscription agent. See The Rights Offering Guaranteed Delivery Procedures.
No Revocation Permitted	<b>Unitholders who have exercised their rights pursuant to the rights offering may NOT revoke or withdraw their exercise of their rights.</b>
Subscription Agent	LaSalle Bank National Association, 135 S. LaSalle Street, Suite 1811, Chicago, Illinois 60603, Telephone: (800) 246-5761, Menu Option 2, Facsimile: (312) 904-2079, Attention: Corporate Trust Operations.
Material Tax Consequences	A U.S. rightsholder generally will not recognize taxable income in connection with the issuance or exercise of rights. However, we may be required to make special allocations of income and gain or loss and deduction to holders of common units acquired by exercising rights in order to cause the capital account associated with each acquired unit to be equivalent to the capital account of all other common units. For a summary of the material U.S. federal income tax consequences of holding units acquired by exercising rights, see Material Tax Consequences.
Use of Proceeds	We will receive approximately \$39.375 million of proceeds before deducting any expenses from the recapitalization (assuming full

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unitholder participation). These recapitalization expenses are estimated to be \$6.5 million. We plan to use the net proceeds we receive from the rights offering, together with \$16.875 million in proceeds from the issuance of an aggregate of 6,750,000 common units to Kestrel and M2, and additional funds from operations, to repurchase at least \$60 million and, at our option, up to approximately \$73.1 million in face amount of our senior notes (assuming full noteholder participation in the senior notes tender offer). Any additional proceeds that we receive in connection with the exercise of M2's standby commitment at \$2.25 per unit will reduce the amount of funds from operations that are needed to repurchase senior notes. As of the date of this prospectus, the holders of an aggregate of approximately \$5.8 million in senior notes have not yet agreed to tender their notes in the tender offer. The principal amount of any senior notes, plus any interest and premium payments that we are required to make in respect of senior notes tendered for repurchase in the change of control repurchase offer, will reduce on a dollar-for-dollar basis the amount of senior notes that we shall repurchase for cash in connection with the closing of the recapitalization.

**No Recommendation**

Neither we nor the board of directors of our general partner has made any recommendation as to whether you should exercise your rights. You should decide whether to subscribe for common units or simply take no action with respect to your rights, based upon your own assessment of the risks in making an additional investment in us. See Risk Factors, The Rights Offering No Recommendations to Rightsholders, Information Regarding Kestrel Heat Interests of the Proposed Executive Officers and Directors in the Recapitalization and Conflicts of Interest.

**Summary of the Common Units**

*The following summary of the common units and other partnership interests gives effect to the adoption of the second amended and restated agreement of limited partnership in connection with the closing of the recapitalization: See Amendments to the Partnership Agreement Comparison of the Star Gas Partnership Agreement Before and After the Recapitalization.*

**Units to be Outstanding After the Recapitalization**

Approximately 75,774,336 common units, representing a combined 99.6% limited partner interest, and 325,729 general partner units, representing a combined 0.4% general partner interest.

**Requirement to Distribute Available Cash**

Within 45 days following the end of each quarter commencing with the quarter beginning October 1, 2008, or if we elect to commence making distributions sooner, the quarter in which any distribution of available cash is made, Star Gas Partners is required to distribute 100% of its available cash with respect to such quarter to partners as of the record date selected by the general partner in its reasonable discretion. Star Gas Partners has no obligation to distribute available cash through the quarter ending September 30, 2008 and currently has no intention of making any such distributions.



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Definition of Available Cash	Available cash for any quarter will continue to consist of all cash on hand at the end of that quarter, as adjusted for reserves. The general partner has broad discretion in establishing reserves.
Minimum Quarterly Distribution	\$0.0 through the quarter ending September 30, 2008, or if we elect to commence making distributions sooner, the quarter in which any distribution of available cash is made, and \$0.0675 per unit per quarter, or \$0.27 per unit per year, thereafter.
First Target Distribution Level	\$0.1125 per unit per quarter or \$0.45 per unit per year.
Distribution of Available Cash from Operating Surplus	<p>Available cash from operating surplus with respect to any quarter will be distributed in the following manner:</p> <p>First, 100% to the common units, pro rata, until we distribute to each common unit the minimum quarterly distribution of \$0.0675;</p> <p>Second, 100% to the common units, pro rata, until we distribute to each common unit any arrearages in payment of the minimum quarterly distribution on the common units for prior quarters;</p> <p>Third, 100% to the general partner units, pro rata, until we distribute to each general partner unit the minimum quarterly distribution of \$0.0675;</p> <p>Fourth, 90% to the common units, pro rata, and 10% to the general partner units, pro rata, until we distribute to each common unit the first target distribution of \$0.1125; and</p> <p>Thereafter, 80% to the common units, pro rata, and 20% to the general partner units, pro rata.</p>
Subordination Period	Because all senior subordinated units and junior subordinated units will convert into common units as part of the recapitalization, the subordination period will end. All outstanding limited partner units will be common units.
Voting	<p>Approval of a majority of the outstanding common units, including common units owned by the general partner and its affiliates, is required for the following:</p> <p>certain amendments to our partnership agreement;</p> <p>the merger of our partnership or the sale of all or substantially all of our assets; and</p> <p>the dissolution of our partnership.</p>

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Immediately following the closing of the recapitalization, the Kestrel entities will own approximately 8.9% of the issued and outstanding common units if the rights offering is fully subscribed for by existing common unitholders or 34.9% of the issued and outstanding common units if none of the units offered in the rights offering are purchased by existing common unitholders.

**Table of Contents****Summary Consolidated Historical Financial and Operating Data**

The following table sets forth our summary consolidated financial information that has been derived from (i) our audited consolidated statements of operations and cash flows for each of the years ended September 30, 2003, 2004 and 2005 and our consolidated balance sheets as of September 30, 2004 and 2005 included in our Annual Report on Form 10-K for the fiscal year ended September 30, 2005, as amended by Form 10-K/A (the Annual Report on Form 10-K/A), incorporated by reference in this prospectus and (ii) the unaudited condensed consolidated statements of operations and cash flows for our business for the three months ended December 31, 2004 and 2005 and the balance sheet data as of December 31, 2005 included in our Quarterly Report on Form 10-Q/A incorporated by reference in this prospectus. You should read this financial information in conjunction with Selected Historical Financial and Operating Data and Management's Discussion and Analysis of Financial Condition and Results of Operations and our historical consolidated financial statements and notes incorporated by reference in this prospectus from our Annual Report on Form 10-K/A for the fiscal year ended September 30, 2005 and our Quarterly Report on Form 10-Q/A for the quarter ended December 31, 2005 incorporated by reference in this prospectus. The information set forth below is not necessarily indicative of our future results or financial position.

(in thousands, except per unit data)	Fiscal Years Ended September 30,			Three Months Ended December 31,	
	2003	2004	2005	2004	2005
<b>Statement of Operations Data:</b>					
Sales	\$ 1,102,968	\$ 1,105,091	\$ 1,259,478	\$ 350,694	\$ 414,381
Costs and expenses:					
Cost of sales	793,543	799,055	983,779	281,278	319,667
Delivery and branch expenses	217,244	232,985	231,581	65,480	59,426
Depreciation and amortization expenses	35,535	37,313	35,480	9,122	8,485
General and administrative expenses	39,763	19,937	43,418	15,842	6,366
Goodwill impairment charge			67,000		
Operating income (loss)	16,883	15,801	(101,780)	(21,028)	20,437
Interest expense, net	(29,530)	(36,682)	(31,838)	(10,492)	(6,682)
Amortization of debt issuance costs	(2,038)	(3,480)	(2,540)	(715)	(631)
Gain (loss) on redemption of debt	212		(42,082)	(42,082)	
Income (loss) from continuing operations before income taxes	(14,473)	(24,361)	(178,240)	(74,317)	13,124
Income tax expense	1,200	1,240	696	331	250
Income (loss) from continuing operations	(15,673)	(25,601)	(178,936)	(74,648)	12,874
Income (loss) from discontinued operations, net of income taxes	19,786	20,276	(4,552)	(4,552)	
Gain (loss) on sales of discontinued operations, net of income taxes		(538)	157,560	153,644	
Income (loss) before cumulative effects of changes in accounting principles	4,113	(5,863)	(25,928)	74,444	12,874
Cumulative effects of change in accounting principle:					
Adoption of SFAS No. 142	(3,901)				
Change in inventory pricing method					(344)
Net income (loss)	\$ 212	\$ (5,863)	\$ (25,928)	\$ 74,444	\$ 12,530
Weighted average number of limited partner units:					
Basic	32,659	35,205	35,821	35,756	35,903
Diluted	32,767	35,205	35,821	35,756	35,903
<b>Per Unit Data:</b>					
Basic and diluted income (loss) from continuing operations per unit (a)	\$ (0.48)	\$ (0.72)	\$ (4.95)	\$ (2.07)	\$ 0.36

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Basic and diluted net income (loss) per unit (a)	\$ 0.01	\$ (0.16)	\$ (0.72)	\$ 2.06	\$ 0.35
Cash distribution declared per common unit	\$ 2.30	\$ 2.30	\$	\$	\$
Cash distribution declared per senior sub. unit	\$ 1.65	\$ 1.73	\$	\$	\$
Cash distribution declared per junior sub. unit	\$ 1.15	\$	\$	\$	\$
Cash distribution declared per general partner unit	\$ 1.15	\$	\$	\$	\$
<b>Balance Sheet Data (end of period):</b>					
Current assets	\$ 211,109	\$ 234,171	\$ 311,432	\$ 393,630	\$ 322,026
Total assets	\$ 975,610	\$ 960,976	\$ 629,261	\$ 809,580	\$ 634,178
Long-term debt	\$ 499,341	\$ 503,668	\$ 267,417	\$ 268,582	\$ 267,339
Partners' Capital	\$ 189,776	\$ 169,771	\$ 145,108	\$ 219,167	\$ 116,767

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(in thousands, except per unit data)	Fiscal Years Ended September 30,			Three Months Ended December 31,	
	2003	2004	2005	2004	2005
<b>Summary Cash Flow Data:</b>					
Net cash provided by (used in) operating activities	\$ 15,365	\$ 13,669	\$ (54,915)	\$ (151,895)	\$ (112,449)
Net cash provided by (used in) investing activities	\$ (48,395)	\$ 6,447	\$ 467,431	\$ 463,705	\$ (2,546)
Net cash provided by (used in) financing activities	\$ 48,049	\$ (19,874)	\$ (306,694)	\$ (192,708)	\$ 25,064
<b>Other Data:</b>					
EBITDA (b)	\$ 52,630	\$ 53,114	\$ (108,382)	\$ (53,988)	\$ 28,922
Heating oil segment s retail gallons sold	567,024	551,612	487,300	142,274	131,270

- (a) Income (loss) from continuing operations per unit is computed by dividing the limited partners' interest in income (loss) from continuing operations by the weighted average number of limited partner units outstanding. Net income (loss) per unit is computed by dividing the limited partners' interest in net income (loss) by the weighted average number of limited partner units outstanding.
- (b) EBITDA from continuing operations should not be considered as an alternative to net income (as an indicator of operating performance) or as an alternative to cash flow (as a measure of liquidity or ability to service debt obligations), but provides additional information for evaluating our ability to make the minimum quarterly distribution. The working capital facility and the senior notes impose certain restrictions on our ability to pay distributions to unitholders.

The definition of EBITDA set forth above may be different from that used by other companies. EBITDA from continuing operations is calculated as follows:

Statement of Operations Data (in thousands)	Fiscal Years Ended September 30,			Three Months Ended December 31,	
	2003	2004	2005	2004	2005
Income (loss) from continuing operations	\$ (15,673)	\$ (25,601)	\$ (178,936)	\$ (74,648)	\$ 12,874
Plus:					
Income tax expense	1,200	1,240	696	331	250
Amortization of debt issuance cost	2,038	3,480	2,540	715	631
Interest expense, net	29,530	36,682	31,838	10,492	6,682
Depreciation and amortization	35,535	37,313	35,480	9,122	8,485
<b>EBITDA from continuing operations</b>	<b>52,630</b>	<b>53,114</b>	<b>(108,382)</b>	<b>(53,988)</b>	<b>28,922</b>
Add/(subtract)					
Income tax expense	(1,200)	(1,240)	(696)	(331)	(250)
Interest expense, net	(29,530)	(36,682)	(31,838)	(10,492)	(6,682)
Unit compensation expense (income)	9,001	(4,382)	(2,185)	(2,094)	
Provision for losses on accounts receivable	6,601	7,646	9,817	1,721	1,977
Gain on sales of fixed assets, net	(52)	(281)	(43)	(73)	427
Goodwill impairment charge			67,000		
(Gain)/loss on redemption of debt	(212)		42,082	42,082	
Unrealized loss on derivative instruments, net	306	1,673	2,144	3,941	1,089
Change in operating assets and liabilities	(22,179)	(6,179)	(32,814)	(132,661)	(137,932)
<b>Net cash provided by (used in) operating activities</b>	<b>\$ 15,365</b>	<b>\$ 13,669</b>	<b>\$ (54,915)</b>	<b>\$ (151,895)</b>	<b>\$ (112,449)</b>



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The following summary selected unaudited pro forma condensed consolidated statement of operations for the fiscal year ended September 30, 2005 and the three months ended December 31, 2005 assumes the recapitalization occurred on October 1, 2004 and October 1, 2005, respectively. The selected unaudited pro forma condensed consolidated balance sheet data as of December 31, 2005 assumes the recapitalization occurred on December 31, 2005. You should not rely on the pro forma financial information as being indicative of the historical results that we would have had or the future results that we will experience after the recapitalization. See Unaudited Condensed Pro Forma Financial Information.

The Pro Forma column of the table represents the recapitalization assuming the repayment of approximately \$73.1 million in senior notes (assuming full noteholder participation in the senior notes tender offer) and the conversion of approximately \$26.9 million of senior notes into common units. As of the date of this prospectus, the holders of an aggregate of approximately \$5.8 million in senior notes have not yet agreed to tender their notes in the tender offer. The principal amount of any senior notes, plus any interest and premium payments that we are required to make in respect of senior notes tendered for repurchase in the change of control repurchase offer, will reduce on a dollar-for-dollar basis the amount of senior notes that we shall repurchase for cash in connection with the closing of the recapitalization.

(in thousands, except per unit data)	Fiscal Year Ended September 30, 2005	Three Months Ended December 31, 2005
	Pro Forma	Pro Forma
	(unaudited)	(unaudited)
Sales:		
Product	\$ 1,071,270	\$358,869
Installations and service	188,208	55,512
Total sales	1,259,478	414,381
Cost and expenses:		
Cost of product	786,349	261,972
Cost of installations and service	197,430	57,695
Delivery and branch expenses	231,581	59,426
Depreciation and amortization expenses	35,480	8,485
General and administrative expenses	43,418	6,366
Goodwill impairment charge	67,000	
Operating income (loss)	(101,780)	20,437
Interest expense	(26,016)	(5,483)
Interest income	3,606	858
Amortization of debt issuance costs	(2,230)	(553)
Loss on redemption of debt	(42,082)	
Income (loss) from continuing operations before income taxes	(168,502)	15,259
Income tax expense	696	250
Income (loss) from continuing operations	\$ (169,198)	\$ 15,009
General Partner's interest income (loss) from continuing operations	\$ (726)	\$ 64
Limited Partners' interest income (loss) from continuing operations	\$ (168,472)	\$ 14,945

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Basic and diluted income (loss) from continuing operations per Limited Partner Unit:	\$ (2.23)	\$ 0.20
Weighted average number of Limited Partner units outstanding:		
Basic and Diluted	75,692	75,774



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	<b>December 31, 2005</b>	<b>December 31, 2005</b>
	<b>Actual</b>	<b>Pro Forma</b>
<b>Balance Sheet Data (end of period)</b>		
Current assets	\$ 322,026	\$ 319,919
Total assets	634,178	629,835
Long-term debt	267,339	166,492
Total partners' capital	116,767	192,362
	<b>Fiscal Year Ended September 30, 2005</b>	<b>Three Months Ended December 31, 2005</b>
	<b>Pro Forma</b>	<b>Pro Forma</b>
	<b>(In thousands)</b>	<b>(In thousands)</b>
<b>Summary Cash Flow Data</b>		
Net cash used in operating activities	\$ (44,455)	\$ (109,893)
Net cash provided by (used in) investing activities	467,431	(2,546)
Net cash provided by (used in) financing activities	(330,076)	4,155

**Other Data**

EBITDA (see footnote (b) to the Summary Consolidated Historical Financial and Operating Data table above) is calculated as follows:

	<b>Fiscal Year Ended September 30, 2005</b>	<b>Three Months ended December 31, 2005</b>
	<b>Pro Forma</b>	<b>Pro Forma</b>
Pro Forma income (loss) from continuing operations	\$ (169,198)	\$ 15,009
Plus:		
Income tax expense	696	250
Amortization of debt issuance cost	2,230	553
Interest expense, net	22,410	4,625
Depreciation and amortization	35,480	8,485
Pro Forma EBITDA from continuing operations	\$ (108,382)	\$ 28,922

**2006 Forecast of Star Gas Partners**

Our management prepared a forecast for fiscal 2006 that was provided to Kestrel. The forecast was not prepared with a view to public disclosure. This forecast is included in this prospectus only because it was provided to Kestrel in connection with the negotiation of the unit

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purchase agreement and has been included in our proxy statement relating to the recapitalization. The forecast was prepared in October 2005 as of September 30, 2005 and has not been updated to give effect to any developments since that time. See **Recent Results** and **Risk Factors**. The forecast was prepared by, and is the responsibility of, management of Star Gas Partners. No independent registered public accounting firm examined, compiled or applied any procedures for the projections or expressed any opinion or provided any kind of assurance on the forecast.

While presented with numerical specificity, the forecast is based on a variety of assumptions relating to the business Star Gas Partners that, although considered appropriate by Star Gas Partners at the time, may not be realized. The principal assumptions are discussed below. Moreover, the forecast and the assumptions upon which it is based are subject to significant uncertainties and contingencies, many of which are beyond the control of management of Star Gas Partners. Consequently, the forecast and the underlying assumptions are necessarily speculative in nature and inherently imprecise, and there can be no assurance that the forecasted financial results

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will be realized. It is expected that there will be differences between actual and forecasted results, and actual results are likely to vary materially from those shown. None of Star Gas Partners, our Board of Directors, nor any of their affiliates or advisors intends to update or otherwise revise the forecast.

The inclusion of the forecast in this prospectus should not be regarded as an indication that Star Gas Partners, our Board of Directors, Kestrel or any of their affiliates or advisors considers the forecast likely to be an accurate prediction of future results. Star Gas Partners' unitholders are cautioned not to place undue reliance on the forecast, which should be read in conjunction with information relating to the business, assets and financial condition of Star Gas Partners included or incorporated by reference herein.

The forecast contains forward-looking information and is subject to a number of risks discussed elsewhere in this prospectus. See **Risk Factors** and **Forward-Looking Statements**. These risks are likely to cause actual results in the future to differ significantly from results expressed or implied in the forecast.

The forecast set forth below is the most recent version of the forecast provided to Kestrel. Star Gas Partners believes that discussion of the earlier version would not add materially to the information provided here.

EBITDA from continuing operations should not be considered as an alternative to net income (as an indicator of operating performance) or as an alternative to cash flow (as a measure of liquidity or ability to service debt obligations), but provides additional information for evaluating our ability to make the minimum quarterly distribution. The working capital facility and the senior notes impose certain restrictions on our ability to pay distributions to unitholders. This definition of EBITDA may be different from that used by other companies.

### *2006 Forecast of Star Gas Partners General Assumptions*

For fiscal 2006, volume of home heating oil sold is assumed to decline by 20.0 million gallons, or 4.1%, to 467.3 million gallons as compared to 487.3 million gallons sold in fiscal 2005. This assumption was based upon a 4.5% net customer loss assumption in fiscal 2006 and adjustment to match the most recent 10-year average weather. No incremental customer conservation was assumed and volume assumptions follow customer consumption behavior exhibited in fiscal 2005.

For fiscal 2006, home heating oil margins are assumed to be 59 cents per gallon, which represents an increase of 3.3 cents per gallon over the level achieved in fiscal 2005 of 55.7 cents per gallon.

Service and installation revenues are assumed to increase due to a significant reduction in service contract discounting coupled with other price increases.

Projected operating expenses include the incremental effect of various cost reduction efforts undertaken in the second half of fiscal 2005. Headcount reductions and other cost curtailments are assumed to more than offset fiscal 2006 wage, medical and benefit cost increases. Operating expense assumes only recurring business overhead costs. The forecast excludes the potential restructuring related expenses incurred in

connection with the recapitalization, which are currently estimated at \$6.5 million.

Interest expense is a status quo estimate and does not reflect prospective savings from the debt reduction which would occur in the Kestrel proposed recapitalization. The prospective savings from such debt reduction will range from \$8.7 million to \$10.3 million depending on the amount of senior notes which participate in the senior notes tender offer and change of control repurchase offer.

A contingency of \$4.1 million was established to offset current market risks. The contingency was established to offset the risk of additional attrition, conservation and margin compression due to higher than historical pricing levels and increased customer price sensitivity and awareness.

**Table of Contents****Consolidated Statements of Operations**

<u>(in thousands)</u>	<u>Fiscal 2006</u>
Sales:	
Product	\$ 1,189,545
Installation and services	190,049
	<hr/>
Total sales	1,379,594
Cost and expenses	
Cost of product	897,645
Cost of installations and service	193,649
Delivery and branch expenses	216,045
Depreciation and amortization	33,233
General and administrative expenses	25,155
Contingency	4,100
	<hr/>
Operating income	9,767
Net interest expense	30,060
Amortization of debt issuance costs	2,427
	<hr/>
Loss from operations before income tax	(22,720)
	<hr/>
Income tax expense	1,500
	<hr/>
Net loss	<u>\$ (24,220)</u>

**EBITDA**

<u>(in thousands)</u>	
Net loss	\$ (24,220)
Plus:	
Income taxes	1,500
Amortization of debt issuance costs	2,427
Net interest expense	30,060
Depreciation and amortization	33,233
	<hr/>
EBITDA	<u>\$ 43,000</u>

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**RISK FACTORS**

*You should consider carefully the risk factors discussed below, as well as all other information in this prospectus and the documents incorporated herein by reference before you decide to exercise rights. Investing in our common units is speculative and involves significant risk. Any of the risks described in this prospectus could impair our business, financial condition and operating results, could cause the trading price, if any, of the common units to decline or could result in a partial or total loss of your investment.*

**Risks Related to the Recapitalization, Including the Rights Offering**

*If we terminate the rights offering, neither we nor the subscription agent will have any obligation to you except to return your subscription payments.*

We may in our sole discretion decide not to continue with the rights offering or to terminate the rights offering prior to the Expiration Time. This decision would be based upon various factors, including market conditions. We have no present intention to terminate the rights offering, but we are reserving the right to do so in the event that unforeseen circumstances occur between the date of this prospectus and the expiration of the rights offering. If we terminate the rights offering, neither we nor the subscription agent will have any obligation to you with respect to the rights, except to return your subscription payments, without interest or deduction.

*Once you exercise your rights, you may not revoke your commitment.*

Once you exercise your rights, you may not revoke your commitment. Therefore, even if circumstances arise after you have subscribed in the offering that change your mind about investing in our common units, you will nonetheless be legally bound to proceed.

*You should not consider the subscription price of our common units as an indication of the value of our partnership or our common units.*

The subscription price of our common units may not reflect the value of our partnership or our common units. The subscription price was determined by our board of directors primarily as a result of negotiations with the Kestrel entities. The subscription price does not necessarily bear any relationship to the book value of our assets, historical or future cash flows, financial condition, recent or historical unit prices or any other established criteria for valuation. We cannot assure you that our common units will trade at prices equal to or in excess of the subscription price at any time after the date of this prospectus.

At December 2, 2005, the last trading day prior to our public announcement of the recapitalization transaction, the closing sales price of the common units was \$1.32. On April 5, 2006, the last trading day prior to the date of this prospectus, the closing sales price per common unit was \$2.61. Unitholders are urged to obtain a current quotation for the common units.

***Unitholders who do not fully exercise their rights will have their interests diluted by unitholders who do exercise their rights (or by M2 pursuant to its standby commitment) and they will be diluted even if they do.***

The rights offering will result in our issuance of an additional 19,687,500 common units. If you choose not to fully exercise your rights, your relative ownership interests in us would be diluted, although even those unitholders who exercise their rights will experience dilution as a result of the issuance of approximately 43,608,808 new common units (including the rights offering units) in connection with the recapitalization. However, rightsholders who, prior to the Expiration Time, do not exercise their rights, would have their relative ownership interests in us diluted more than if they do exercise.

***Each common unitholder will experience substantial dilution in his interest in Star Gas Partners.***

As a result of the issuance of units to Kestrel and the issuance of units in the rights offering, the issuance of additional units to the noteholders in conversion of senior notes into common units and the conversion of the

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senior subordinated units and junior subordinated units into common units, the number of common units will increase from 32,165,528 to approximately 75,774,336, representing a substantial dilution of the common unitholders' existing interest. The recapitalization will also result in a termination of the subordination period during which certain issuances of additional units required a unitholder vote. Consequently, there will be no limit in the partnership agreement on the number of additional limited partner interests, including units senior to the common units, that we may issue at any time without the approval of our unitholders. As a result of this dilution and the possible future issuance of additional equity securities:

each common unitholder's proportionate ownership interest in us will decrease;

the amount of cash available for distribution on each unit will decrease (without taking into account the additional cash that would be available as a result of the reduction in interest expense in connection with the repayment or conversion of up to \$100 million of senior notes, assuming full noteholder participation in the senior notes tender offer);

the common units may be subordinated as to distributions and voting rights given to new senior units we may decide to issue in the future, although we do not have any present intention to issue senior units;

the relative voting strength of each previously outstanding unit will be diminished; and

the market price of the common units may decline.

However, common unitholders who participate in the rights offering would be able to reduce the dilution in their unit holdings.

Prior to the recapitalization, the common units represented approximately 88.8% of the total number of units outstanding. Following the recapitalization, if all rightsholders exercise their rights in this rights offering, our existing common unitholders would own common units representing approximately 68.1% of the total number of units outstanding. However, if none of the rightsholders exercise their rights in this rights offering and M2 is issued the 19,687,500 common units offered to the rightsholders hereunder pursuant to its standby commitment, our existing common unitholders would own common units representing approximately 42.3% of the total number of units outstanding.

***Accrued and unpaid arrearages in the payment of the minimum quarterly distribution on the common units will be eliminated.***

Under our partnership agreement as currently in effect, during the subordination period, no distributions can be made on the subordinated units until all accrued and unpaid arrearages in the payment of the minimum quarterly distribution on the common units have been paid. As of February 14, 2006, the amount of accrued and unpaid arrearages in the payment of the minimum quarterly distribution on the common units was \$111.0 million, or \$3.45 per common unit. Assuming that the number of outstanding common units remained at 32,165,528 and that we did not distribute any available cash from operating surplus, these arrearages would increase by \$18.5 million per quarter, or \$0.575 per common unit. As a result of the recapitalization, all accrued and unpaid arrearages on the common units would be eliminated. Consequently, the preference of the existing common unitholders to cash distributions in that amount would be eliminated.

***We have substantially lowered the minimum quarterly distribution and the first target distribution, which will make it easier for the general partner units to receive incentive distributions.***



Under our partnership agreement as currently in effect, the senior subordinated units, junior subordinated units and general partner units are not entitled to receive incentive distributions in a quarter until the first target distribution of \$0.604 per unit has been distributed on each common unit. Under the proposed amendments to our partnership agreement, commencing with the quarter beginning October 1, 2008, or, if we elect to commence making distributions sooner, the quarter in which any distribution of available cash is made, the new general

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partner units in the aggregate will be entitled to receive 10% of the cash distributions in a quarter once each common unit and general partner unit has received the minimum quarterly distribution of \$.0675 for that quarter, plus any arrearages on the common units from prior quarters, and 20% of the cash distributions in a quarter once each common unit and general partner unit has received \$.1125 for that quarter, plus any arrearages on the common units from prior quarters. See Amendments to the Partnership Agreement Comparison of the Star Gas Partnership Agreement Before and After the Recapitalization. Thus, the ability of the general partner units to receive incentive distributions has been enhanced in several ways:

The general partner units are entitled to incentive distributions once the minimum quarterly distribution has been paid on the common units and general partner units, as opposed to only after the first target distribution has been paid under the existing partnership agreement.

The minimum quarterly distribution and the first target distribution have been substantially reduced. The minimum quarterly distribution has been reduced from \$0.575 to \$0.0 for each quarter through September 30, 2008, or if we elect to commence making distributions sooner, the first quarter in which a distribution of available cash is made, and to \$0.0675 thereafter, representing an 88% decrease. The first target distribution has been reduced from \$0.604 to \$.1125 per unit, representing an 81% decrease.

***We are not required to, and currently do not intend to, distribute any available cash through the quarter ending September 30, 2008.***

The partnership agreement amendments provide that we are not obligated to distribute available cash through the quarter ending September 30, 2008. We currently do not intend to make distributions of available cash during this period, even if we have available cash to distribute. Also, if we accumulate available cash during this period, it will be easier for us to make distributions on the general partner units after this period than if we had distributed available cash each quarter.

***If our use of the net proceeds from the sale of the propane segment does not comply with the terms of the indenture for the senior notes, we may be subject to liability to the noteholders, which would have a material adverse effect on our ability to continue as a going concern.***

On December 17, 2004, we completed the sale of our propane segment for a purchase price of \$481.3 million, without assumption of the propane segment's indebtedness for borrowed money at the time of sale. Pursuant to the terms of the indenture relating to our senior notes, we were permitted, within 360 days of the sale, to apply the net proceeds of the sale of the propane segment either to reduce our indebtedness or the indebtedness of a restricted subsidiary, or to make an investment in assets or capital expenditures useful to our or any subsidiary's business. To the extent any net proceeds that were not so applied exceeded \$10 million (referred to in this prospectus as excess proceeds), the indenture requires us to make an offer to all holders of notes to purchase for cash that number of notes that may be purchased with excess proceeds at a purchase price equal to 100% of the principal amount of notes plus accrued and unpaid interest to the date of purchase.

After repayment of certain debt and transaction expenses, the net proceeds from the propane segment sale were approximately \$156.3 million. As of the closing of the propane sale and application of the proceeds, the amount of net proceeds not applied in excess of \$10 million was \$146.3 million. As of September 30, 2005, the heating oil segment had utilized \$53.1 million of the proceeds to invest in working capital assets, purchase capital assets and repay long-term debt, which reduced the amount available to repurchase notes to \$93.2 million. As of December 2, 2005, the heating oil segment had used all of the remaining excess proceeds.

Our board of directors and management considered, based on informal communications with certain noteholders and their counsel, that certain noteholders might take the position that the use of net proceeds to invest in working capital assets was not a permitted use under the indenture.

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Based upon the advice of counsel, we disagreed with this position. However, we recognized that if we were unsuccessful in defending our position, this would constitute an event of default if declared by either the holders of 25% in principal amount of the senior

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notes or by the trustee under the indenture, and in such event all amounts due under the senior notes would become immediately due and payable. An acceleration of our senior notes would have a material adverse effect on our ability to continue as a going concern. The report of our independent registered public accounting firm on our consolidated financial statements as of September 30, 2005 and 2004, and for the three years ended September 30, 2005, includes an explanatory paragraph with respect to the impact of this matter on our ability to continue as a going concern if this matter is resolved adversely to us. We have reached an agreement with the holders of approximately 97% in aggregate principal amount of the senior notes to resolve this matter, which is subject to our completing the proposed recapitalization, of which there can be no assurance.

### ***Affiliates of the general partner will now be able to vote on all matters.***

Under the existing partnership agreement, during the subordination period the votes of the general partner and its affiliates were excluded in determining a quorum for, and the votes on, any matter requiring the approval of a unit majority, which included certain amendments to our partnership agreement; the merger of our partnership or the sale of all or substantially all our assets; and the dissolution of our partnership. Due to the mandatory conversion of the senior and junior subordinated units into common units, the subordination period will end. Consequently, after the recapitalization, the general partner and its affiliates will be able to vote their units on all matters brought before the unitholders. Immediately following the closing of the recapitalization, the Kestrel entities will own approximately 8.9% of the issued and outstanding common units if the rights offering is fully subscribed for by existing common unitholders or 34.9% of the issued and outstanding common units if none of the units offered in the rights offering are purchased by existing common unitholders.

### ***Possible conflicts of interest were present in negotiating and structuring the recapitalization.***

Certain executive officers and directors of Star Gas have interests in the recapitalization that are different from, and may conflict with, the interests of the public unitholders. Kestrel has proposed that following the closing of the recapitalization, Mr. William P. Nicoletti, the chairman of the board of Star Gas, Mr. Joseph Cavanaugh, the chief executive officer and a director of Star Gas and Mr. Daniel Donovan, the president of Star Gas, would become directors of Kestrel Heat. Mr. Paul Biddelman, Mr. Stephen Russell and Mr. Erik P. Sevin, the other three directors of Star Gas, will not become directors of Kestrel Heat. In addition, if the recapitalization is consummated, Mr. Cavanaugh, Mr. Donovan and Mr. Richard Ambury, the chief financial officer, treasurer and secretary of Star Gas, would continue to be employed by us under the terms of their current employment arrangements.

The unit purchase agreement provides in general that Kestrel will cause Star Gas Partners to maintain, for a period of six years after the completion of the transaction, the current indemnification agreements and provisions for Star Gas officers and directors and the current policies of directors and officers liability insurance maintained by Star Gas Partners, or policies of at least the same coverage and amounts containing terms and conditions that are no less advantageous, with respect to claims arising from facts or events that occurred on or before the date of the completion of the transaction.

The membership interests in Star Gas are owned by Mr. Sevin, Ms. Audrey L. Sevin and Hanseatic Americas, Inc. Mr. Sevin is a director of Star Gas. Star Gas and its members own an aggregate of 314,305 senior subordinated units and 345,364 junior subordinated units, all of which will be converted into common units in connection with the proposed recapitalization. Mr. Biddelman, who is a director of Star Gas, is an executive officer of Hanseatic Corporation, the sole managing member of Hanseatic Americas, LDC, which is the indirect parent of Hanseatic Americas, Inc. Mr. Biddelman beneficially owns an approximately 10% equity interest in Hanseatic Americas, Inc., and persons unaffiliated with Mr. Biddelman beneficially own an approximately 80% equity interest in Hanseatic Americas, Inc.

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In addition, the executive officers and directors of Star Gas (excluding Mr. Sevin) own an aggregate of 18,561 senior subordinated units that will be converted into common units in connection with the proposed recapitalization.

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Kestrel has acknowledged that Star Gas Partners is required to reimburse Star Gas for amounts that are payable by Star Gas to Mr. Sevin under his agreement dated March 7, 2005 and Kestrel has agreed to cause Star Gas Partners to continue to make such reimbursement without offsets, defenses or counterclaims, except that Star Gas Partners shall have such defenses as may become available to Star Gas pursuant to such agreement. See Risk Factors, Information Regarding Kestrel Heat Interests of the Proposed Executive Officers and Directors in the Recapitalization and Conflicts of Interest.

*Our noteholders and affiliates of Kestrel may sell common units in the public market, which sales could have an adverse impact on the trading price of our common units.*

After the recapitalization, our senior noteholders will own 13,433,962 (subject to adjustment based on rounding) common units and affiliates of Kestrel will own between 6,750,000 common units and 26,437,500 common units. We have granted the consenting noteholders certain registration rights for these units and our partnership agreement would provide Kestrel and its affiliates with certain registration rights for these units. The sale of these units in the public market could have an adverse impact on the price of the common units.

## **Risks Inherent in an Investment in Star Gas Partners**

*The continuation of high wholesale energy costs may adversely affect our liquidity.*

Under our revolving credit facility, as amended, we may borrow up to \$260 million, which increases to \$310 million during the peak winter months from December through March of each year (subject to borrowing base limitations and a coverage ratio), for working capital purposes subject to maintaining availability (as defined in the credit agreement) of \$25 million or a fixed charge coverage ratio of not less than 1.1 to 1.0.

Recent dynamics of the heating oil industry have adversely impacted working capital requirements, principally as follows:

High selling prices require additional borrowing to finance accounts receivable; however, we may borrow only approximately 85% against eligible accounts receivable and 40% to 80% of eligible inventory. In addition we may borrow up to \$35 million against fixed assets and customer lists, which is reduced by \$7.0 million each year over the life of the credit agreement. As of December 31, 2005, the amount included in the borrowing base for fixed assets and customer lists was \$28.0 million.

At present, suppliers are not providing credit terms to us, requiring us to pay in advance for product. Historically, we have enjoyed, on average, two-to three-day credit terms providing additional credit support during the heating season.

Due to our current credit position, our ability to execute certain hedging strategies has been curtailed, which we anticipate will require us to purchase a greater proportion of New York Mercantile Exchange ( NYMEX ) futures contracts to implement our hedging strategy than we have in the past. These contracts require an initial margin at the time of purchase and we are required to fund maintenance margins based on daily market adjustments should the market price of home heating oil decrease. The payment of these margins, if required, may be well in advance of settlement and will have an adverse impact on liquidity.

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In addition to the foregoing, there is a risk that accounts receivable collection experience may not equal that of prior periods since customers are owing larger amounts which could be outstanding for longer periods of time.

If our credit requirements should exceed the amounts available under our revolving credit facility or should we fail to maintain the required availability, we would not have sufficient working capital to operate our business, which could have a material adverse effect on our financial condition and results of operations.

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***Our substantial debt and other financial obligations could impair our financial condition and our ability to fulfill our debt obligations.***

We had total debt, exclusive of our working capital facility, of approximately \$268.1 million as of December 31, 2005. After giving effect to the recapitalization, we expect to have total pro forma indebtedness (including current maturities) of approximately \$167.2 million and pro forma partners' capital of approximately \$192.4 million at December 31, 2005. See Capitalization and Unaudited Condensed Pro Forma Financial Information. Our substantial indebtedness and other financial obligations could:

impair our ability to obtain additional financing in the future for working capital, capital expenditures, acquisitions or general corporate purposes;

have a material adverse effect on us if we fail to comply with financial and affirmative and restrictive covenants in our debt agreements and an event of default occurs as a result of a failure that is not cured or waived;

require us to dedicate a substantial portion of our cash flow for interest payments on our indebtedness and other financial obligations, thereby reducing the availability of our cash flow to fund working capital and capital expenditures;

limit our flexibility in planning for, or reacting to, changes in our business and the industry in which we operate; and

place us at a competitive disadvantage compared to our competitors that have proportionately less debt.

If we are unable to meet our debt service obligations and other financial obligations, we could be forced to restructure or refinance our indebtedness and other financial transactions, seek additional equity capital or sell our assets. We may then be unable to obtain such financing or capital or sell our assets on satisfactory terms, if at all.

***Since weather conditions may adversely affect the demand for home heating oil, our financial condition is vulnerable to warm winters.***

Weather conditions have a significant impact on the demand for home heating oil because our customers depend on this product principally for space heating purposes. As a result, weather conditions may materially adversely impact our operating results and financial condition. During the peak heating season of October through March, sales of home heating oil historically have represented approximately 75% to 80% of our annual home heating oil volume. Actual weather conditions can vary substantially from year to year, significantly affecting our financial performance. Furthermore, warmer than normal temperatures in one or more regions in which we operate can significantly decrease the total volume we sell and the gross profit realized on those sales and, consequently, our results of operations. For example, in fiscal 2000 and especially fiscal 2002, temperatures were significantly warmer than normal for the areas in which we sell home heating oil, which adversely affected the amount of EBITDA that we generated during these periods. In fiscal 2002, temperatures in our areas of operation were an average of 18.4% warmer than in fiscal 2001 and 18.0% warmer than normal. Average temperatures for January 2006 were 29.3% warmer than January 2005. We purchase weather insurance to help minimize the adverse effect of weather volatility on our cash flows. However, there can be no assurance that this insurance will be adequate to protect us from adverse effects of weather conditions.

***Our operating results will be adversely affected if we experience significant customer losses that are not offset or reduced by customer gains.***



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Our net attrition rates of home heating oil customers for fiscal 2003, 2004 and 2005 were approximately 1.5%, 6.4% and 7.1%, respectively. This rate represents the net of our annual customer loss rate after customer gains, not including acquisitions. For fiscal 2003, 2004 and 2005, gross customer losses were 16.4%, 19.5% and 20%, respectively. Both our gross customer losses and net customer attrition rates have increased since fiscal

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2003. We do not know if the acceleration in our rate of gross customer losses and net customer attrition can be halted. For fiscal 2003, 2004 and 2005, gross customer gains were 14.9%, 13.1% and 12.9%, respectively. The gain of a new customer does not fully compensate for the loss of an existing customer during the first year because of the expenses incurred to acquire a new customer and the higher attrition rate associated with new customers. Customer losses are the result of various factors, including:

supplier changes based primarily on price competition, particularly during periods of high energy costs;

quality of service issues, including those related to our centralized call center;

credit problems; and

customer relocations.

The continuing unprecedented rise and volatility in the price of heating oil has intensified price competition, which has adversely impacted our margins and added to our difficulty in reducing customer attrition. We believe our attrition rate has risen not only because of increased price competition related to the rise in oil prices, but also because of operational problems. Prior to the 2004 winter heating season, we attempted to develop a competitive advantage in customer service and, as part of that effort, centralized a majority of our heating equipment service dispatch and engaged a centralized call center to fulfill telephone requirements for a majority of our home heating oil customers. We experienced difficulties in advancing this initiative during fiscal 2004, which adversely impacted our customer base and costs. In fiscal 2004 and 2005, the customer experience was below the level associated with other premium service providers and below the level of service provided by us in prior years.

We believe that we have identified the problems associated with the centralization efforts and are taking steps to address these issues. We expect that high net attrition rates may continue through fiscal 2006 and perhaps beyond and even to the extent the rate of attrition can be halted, attrition from prior fiscal years will adversely impact net income in the future.

We believe that the increase in net customer attrition over the past two years can be attributed to: (i) a combination of the effect of our premium service/premium price strategy when customer price sensitivity increased due to high energy prices; (ii) our decision in fiscal 2005 to maintain reasonable profit margins going forward in spite of competitors' aggressive pricing tactics; (iii) the lag effect of customer attrition related to service and delivery problems experienced by customers in prior fiscal years; (iv) continued customer dissatisfaction with the centralization of customer care; and (v) tightened customer credit standards.

We have continued to experience net customer attrition during fiscal 2006. During the three months ended December 31, 2005, we lost 1.6% (net) of our home heating oil customer base, as compared to the three months ended December 31, 2004 in which we lost 0.4% (net) of our home heating oil customer base. During the three months ended March 31, 2006, we lost 2.2% (net) of our home heating oil customer base, as compared to the three months ended March 31, 2005 in which we lost 2.0% (net) of our home heating oil customer base. If wholesale prices remain high, we believe the risk of customer losses due to credit problems, especially for commercial customers, may increase and bad debt expense may also increase.

We may not be able to achieve net gains of customers and may continue to experience net customer attrition in the future.

*Sudden and sharp oil price increases that cannot be passed on to customers may adversely affect our operating results.*

The retail home heating oil industry is a margin-based business in which gross profit depends on the excess of retail sales prices over supply costs. Consequently, our profitability is sensitive to changes in the wholesale price of home heating oil caused by changes in supply or other market conditions. These factors are beyond our control and thus, when there are sudden and sharp increases in the wholesale cost of home heating oil, we may not be able to pass on these increases to customers through increased retail sales prices. As of

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December 31, 2005, the wholesale cost of home heating oil, as measured by the closing price on the NYMEX, had increased by 40.5% to \$1.73 per gallon from \$1.23 per gallon as of December 31, 2004. During fiscal 2005, per gallon wholesale home heating oil prices peaked at \$2.18 on September 1, 2005. Wholesale price increases could reduce our gross profits and could, if continuing over an extended period of time, reduce demand by encouraging conservation or conversion to alternative energy sources. In an effort to retain existing accounts and attract new customers, we may offer discounts, which will impact the net per gallon gross margin realized.

*A significant portion of our home heating oil volume is sold to price protected customers and our gross margins could be adversely affected if we are not able to effectively hedge against fluctuations in the volume and cost of product sold to these customers.*

A significant portion of our home heating oil volume is sold to individual customers under an agreement pre-establishing the maximum sales price or a fixed price of home heating oil over a 12-month period. For the fiscal year ended September 30, 2005 and the three months ended December 31, 2005, approximately 48% and 38%, respectively, of our retail home heating oil volume sales were under a price protected plan. The price at which home heating oil is sold to these price protected customers is generally renegotiated prior to the heating season of each year based on current market conditions. We currently purchase futures contracts, swaps and option contracts for a substantial majority of the heating oil that we expect to sell to these price protected customers that have agreements in place in advance and at a fixed or maximum cost per gallon. We purchase these positions when a price protected customer renews his purchase commitment for the next 12 months. We utilize various hedging strategies in order to lock in the per gallon margin for price protected customers. The amount of home heating oil volume that we hedge per price protected customer is based upon the estimated fuel consumption per customer, per month. In the event that the actual usage exceeds the amount of the hedged volume on a monthly basis, we could be required to obtain additional volume at unfavorable margins. In addition, should actual usage be less than the hedged volume we may have excess inventory on hand at unfavorable costs.

*If we do not make acquisitions on economically acceptable terms, our future financial performance will be limited.*

The home heating oil industry is not a growth industry because new housing generally does not use oil heat and increased competition exists from alternative energy sources. A significant portion of our growth in the past decade has been directly tied to our acquisition program. Accordingly, future financial performance will depend on our ability to make acquisitions at attractive prices. We cannot assure that we will be able to identify attractive acquisition candidates in the home heating oil industry in the future or that we will be able to acquire businesses on economically acceptable terms. Factors that may adversely affect home heating oil operating and financial results may limit our access to capital and adversely affect our ability to make acquisitions. Under the terms of our revolving credit facility, the heating oil segment was restricted from making any acquisitions through June 17, 2005 and thereafter individual acquisitions may not exceed \$10 million or an aggregate of \$25 million in any fiscal year. In addition, the heating oil segment is restricted from making any acquisition unless availability (essentially borrowing base availability less borrowings) would be at least \$40 million, on a pro forma basis, during the last 12 month period ending on the date of such acquisition. These restrictions severely limit our ability to make acquisitions. Any acquisition may involve potential risks to us and ultimately to our unitholders, including:

an increase in our indebtedness;

an increase in our working capital requirements;

our inability to integrate the operations of the acquired business;

our inability to successfully expand our operations into new territories;

the diversion of management's attention from other business concerns; and

an excess of customer loss or loss of key employees from the acquired business.

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In addition, acquisitions may be dilutive to earnings and distributions to unitholders and any additional debt incurred to finance acquisitions may among other things, affect our ability to make distributions to our unitholders.

***Because of the highly competitive nature of the retail home heating oil industry, we may not be able to retain existing customers or acquire new customers, which would have an adverse impact on our operating results and financial condition.***

If our home heating oil operations are unable to compete effectively, we may lose existing customers or fail to acquire new customers, which would have a material adverse effect on our results of operations and financial condition.

We compete with heating oil distributors offering a broad range of services and prices, from full service distributors, like us, to those offering delivery only. Competition with other companies in the home heating oil industry is based primarily on customer service and price. It is customary for companies to deliver home heating oil to their customers based upon weather conditions and historical consumption patterns, without the customer making an affirmative purchase decision. Most companies provide home heating equipment repair service on a 24-hour-per-day basis. In some cases, homeowners have formed buying cooperatives to purchase fuel oil from distributors at a price lower than individual customers are otherwise able to obtain. As a result of these factors, it may be difficult to acquire new customers.

We can make no assurances that we will be able to compete successfully. If competitors continue to increase market share by reducing their prices, as we believe occurred in fiscal 2004 and fiscal 2005, our operating results and financial condition could be materially and adversely affected. We also compete for customers with suppliers of alternative energy products, principally natural gas. Competition from alternative energy sources has been increasing as a result of reduced regulation of many utilities, including natural gas and electricity, and the high price of oil. We could face additional price competition from electricity and natural gas as a result of deregulation in those industries. Over the past five years, conversions by our customers from heating oil to natural gas have averaged approximately 1% per year.

The continuing unprecedented rise in the price of heating oil has intensified price competition, which has adversely impacted our product margins and added to our difficulty in reducing customer attrition. We believe our attrition rate has risen not only because of increased price competition related to the rise in oil prices, but also because of operational problems. Prior to the 2004 winter heating season, we attempted to develop a competitive advantage in customer service and, as part of that effort, centralized a majority of our heating equipment service dispatch and engaged a centralized call center to fulfill telephone requirements for the majority of our home heating oil customers. We experienced difficulties in advancing this initiative during fiscal 2004 and 2005, which adversely impacted our customer base and costs. In fiscal 2004 and 2005 the customer experience was below the level associated with other premium service providers and below the level of service provided by us in prior years.

We believe that we have identified the problems associated with these centralization efforts and are taking steps to address these issues. We expect that high net attrition rates may continue through fiscal 2006 and perhaps beyond and even to the extent that the rate of attrition can be halted, attrition in prior fiscal years will adversely impact net income in the future.

***Energy efficiency and new technology may reduce the demand for our products and adversely affect our operating results.***

Increased conservation and technological advances, including installation of improved insulation and the development of more efficient furnaces and other heating devices, have adversely affected the demand for our products by retail customers. Future conservation measures or

technological advances in heating, conservation, energy generation or other devices might reduce demand and adversely affect our operating results.

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*We are subject to operating and litigation risks that could adversely affect our operating results whether or not covered by insurance.*

Our operations are subject to all operating hazards and risks normally incidental to handling, storing, transporting and otherwise providing customers with home heating oil. As a result, we may be a defendant in legal proceedings and litigation arising in the ordinary course of business.

We maintain insurance policies with insurers in amounts and with coverage and deductibles as we believe are reasonable. However, there can be no assurance that this insurance will be adequate to protect us from all material expenses related to potential future claims for remediation costs and personal and property damage or that these levels of insurance will be available in the future at economical prices.

*Our insurance reserves may not be adequate to cover actual losses.*

We self-insure a portion of workers' compensation, automobile and general liability claims. We establish reserves based upon expectations as to what our ultimate liability will be for these claims using developmental factors based upon historical claim experience. We periodically evaluate the potential for changes in loss estimates with the support of qualified actuaries. As of December 31, 2005, we had approximately \$35.3 million of insurance reserves and had issued \$44.9 million in letters of credit for current and future claims. The ultimate settlement of these claims could differ materially from the assumptions used to calculate the reserves, which could have a material effect on our results of operations.

*We are the subject of a class action lawsuit alleging violations of the federal securities laws, which if decided adversely, could have a material adverse effect on our financial condition.*

On or about October 21, 2004, a purported class action lawsuit on behalf of a purported class of unitholders was filed against Star Gas Partners and various subsidiaries and officers and directors in the United States District Court of the District of Connecticut entitled Carter v. Star Gas Partners, L.P., et al., No. 3:04-CV-01766-IBA, et al. Subsequently, 16 additional class action complaints, alleging the same or substantially similar claims, were filed in the same district court: (1) Feit v. Star Gas, et al., Civil Action No. 04-1832 (filed on 10/29/2004), (2) Lila Gold vs. Star Gas, et al., Civil Action No. 04-1791 (filed on 10/22/2004), (3) Jagerman v. Star Gas, et al., Civil Action No. 04-1855 (filed on 11/3/2004), (4) McCole, et al v. Star Gas, et al., Civil Action No. 04-1859 (filed on 11/3/2004), (5) Prokop vs. Star Gas, et al., Civil Action No. 04-1785 (filed on 10/22/2004), (6) Seigle v. Star Gas, et al., Civil Action No. 04-1803 (filed on 10/25/2004), (7) Strunk v. Star Gas, et al., Civil Action No. 04-1815 (filed on 10/27/2004), (8) Harriette S. & Charles L. Tabas Foundation vs. Star Gas, et al., Civil Action No. 04-1857 (filed on 11/3/2004), (9) Weiss v. Star Gas, et al., Civil Action No. 04-1807 (filed on 10/26/2004), (10) White v. Star Gas, et al., Civil Action No. 04-1837 (filed on 10/9/2004), (11) Wood vs. Star Gas et al., Civil Action No. 04-1856 (filed on 11/3/2004), (12) Yopp vs. Star Gas, et al., Civil Action No. 04-1865 (filed on 11/3/2004), (13) Kiser v. Star Gas, et al., Civil Action No. 04-1884 (filed on 11/9/2004), (14) Lederman v. Star Gas, et al., Civil Action No. 04-1873 (filed on 11/5/2004), (15) Dinkes v. Star Gas, et al., Civil Action No. 04-1979 (filed 11/22/2004) and (16) Gould v. Star Gas, et al., Civil Action No. 04-2133 (filed on 12/17/2004) (including the Carter Complaint, collectively referred to herein as the "Class Action Complaints"). The class actions have been consolidated into one action entitled In re Star Gas Securities Litigation, No 3:04CV1766 (JBA).

The class action plaintiffs generally allege that Star Gas Partners violated Sections 10(b) and 20(a) of the Securities Exchange Act of 1934, as amended, and Rule 10-b5 promulgated thereunder, by purportedly failing to disclose, among other things: (1) problems with the restructuring of Star Gas's dispatch system and customer attrition related thereto; (2) that Star Gas's heating oil segment's business process improvement program was not generating the benefits allegedly claimed; (3) that Star Gas was struggling to maintain its profit margins in its heating oil segment; (4) that Star Gas's fiscal 2004 second quarter profit margins were not representative of its ability to pass on heating oil price increases; and



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(5) that Star Gas was facing an inability to pay its debts and that, as a result, its credit rating and ability to obtain future financing was in jeopardy. The class action plaintiffs seek an unspecified amount of compensatory damages including interest against the defendants jointly and

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severally and an award of reasonable costs and expenses. On February 23, 2005, the Court consolidated the Class Action Complaints and heard argument on motions for the appointment of lead plaintiff. On April 8, 2005, the Court appointed the lead plaintiff. Pursuant to the Court's order, the lead plaintiff filed a consolidated amended complaint on June 20, 2005 (the Consolidated Amended Complaint). The Consolidated Amended Complaint named: (a) Star Gas Partners, L.P.; (b) Star Gas LLC; (c) Irik Sevin; (d) Audrey Sevin; (e) Hanseatic Americas, Inc.; (f) Paul Biddelman; (g) Ami Trauber; (h) A.G. Edwards & Sons Inc.; (i) UBS Investment Bank; and (j) RBC Dain Rauscher Inc. as defendants. The Consolidated Amended Complaint added claims arising out of two registration statements and the same transactions under Sections 11, 12(a)(2) and 15 of the Securities Act of 1933, as well as certain allegations concerning the Partnership's hedging practices. On September 23, 2005, defendants filed motions to dismiss the Consolidated Amended Complaint for failure to state a claim under the federal securities laws and failure to satisfy the applicable pleading requirements of the Private Securities Litigation Reform Act of 1995, or PSLRA, and the Federal Rules of Civil Procedure. Plaintiffs filed their response to defendants' motions to dismiss on or about November 23, 2005 and defendants filed their reply briefs on December 20, 2005. The motion is now pending decision by the Court. In the interim, discovery in the matter remains stayed pursuant to the mandatory stay provisions of the PSLRA. While no prediction may be made as to the outcome of litigation, we intend to defend against this class action vigorously.

In the event that the above action is decided adversely to us, it could have a material effect on our results of operations, financial condition and liquidity.

***Our results of operations and financial condition may be adversely affected by governmental regulation and associated environmental and regulatory costs.***

The home heating oil business is subject to a wide range of federal and state laws and regulations related to environmental and other regulated matters. We have implemented environmental programs and policies designed to avoid potential liability and costs under applicable environmental laws. It is possible, however, that we will experience increased costs due to stricter pollution control requirements or liabilities resulting from noncompliance with operating or other regulatory permits. New environmental regulations might adversely impact operations, including underground storage and transportation of home heating oil. In addition, there are environmental risks inherently associated with home heating oil operations, such as the risks of accidental releases or spills. It is possible that material costs and liabilities will be incurred, including those relating to claims for damages to property and persons. Before August 2006 we must implement certain changes to ensure compliance with amended Environmental Protection Agency regulations. We currently estimate that the capital required to effectuate these requirements will range from \$1.0 to \$1.5 million.

***In our acquisition of Meenan, we assumed all of Meenan's environmental liabilities.***

In our acquisition of Meenan Oil Co., L.P. (Meenan), a heating oil company, in August 2001, we assumed all of Meenan's environmental liabilities, including those related to the cleanup of contaminated properties, in consideration of a reduction of the purchase price of \$2.7 million. Subsequent to closing, we established an additional reserve of \$2.3 million to cover potential costs associated with remediating known environmental liabilities, bringing the total reserve to \$5.0 million. As of December 31, 2005, remediation expenses against this reserve have totaled \$3.3 million. While we believe this reserve is adequate, it is possible that the extent of the contamination at issue or the expense of addressing it could exceed our estimates and thus the costs of remediating these known liabilities could materially exceed the amount reserved.

***Conflicts of interest have arisen and could arise in the future as a result of relationships between the general partner and its affiliates on the one hand, and Star Gas Partners and its limited partners, on the other hand.***

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Conflicts of interest have arisen and could arise in the future as a result of relationships between the general partner and its affiliates, on the one hand, and Star Gas Partners or any of the limited partners, on the other hand.

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As a result of these conflicts, the current or any future general partner may favor its own interests and those of its affiliates over the interests of the unitholders. See Conflicts of Interest. The nature of these conflicts is ongoing and includes the following considerations:

Except for Irik P. Sevin, an affiliate of our current general partner who is subject to a non-competition agreement, the general partner's affiliates are not prohibited from engaging in other business or activities, including direct competition with us.

The general partner determines the amount and timing of asset purchases and sales, capital expenditures, borrowings and reserves, each of which can impact the amount of cash, if any, available for distribution to unitholders, and available to pay principal and interest on debt.

The general partner controls the enforcement of obligations owed to Star Gas Partners by the general partner.

The general partner decides whether to retain separate counsel, accountants or others to perform services for Star Gas Partners.

In some instances the general partner may borrow funds in order to permit the payment of distributions to unitholders.

The general partner may limit its liability and reduce its fiduciary duties, while also restricting the remedies available to unitholders for actions that might, without the limitations, constitute breaches of fiduciary duty. Unitholders are deemed to have consented to some actions and conflicts of interest that might otherwise be deemed a breach of fiduciary or other duties under applicable state law.

The general partner is allowed to take into account the interests of parties in addition to Star Gas Partners in resolving conflicts of interest, thereby limiting its fiduciary duty to the unitholders.

The general partner determines whether to issue additional units or other securities of Star Gas Partners.

The general partner determines which costs are reimbursable by us.

Some officers of the general partner, who will provide services to us, may also devote significant time to the businesses of the general partner's affiliates and will be compensated by these affiliates for the services rendered to them. Paul Vermylen, who is proposed to become the Chairman of Kestrel Heat at closing of the recapitalization, serves and is expected to continue to serve as President of Kestrel Energy Partners. Kestrel Energy Partners is a private equity partnership that makes investments in energy-related projects.

The general partner is not restricted from causing us to pay the general partner or its affiliates for any services rendered on terms that are fair and reasonable to us or entering into additional contractual arrangements with any of these entities on our behalf.

***The risk of global terrorism and political unrest may adversely affect the economy and the price and availability of home heating oil and have a material adverse effect on our business, financial condition and results of operations.***

Terrorist attacks, such as the attacks that occurred in New York, Pennsylvania and Washington, D.C. on September 11, 2001, and political unrest in the Middle East may adversely impact the price and availability of home heating oil, our results of operations, our ability to raise capital and

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our future growth. The impact that the foregoing may have on the heating oil industry in general, and on our business in particular, is not known at this time. An act of terror could result in disruptions of crude oil supplies and markets, the source of home heating oil, and its facilities could be direct or indirect targets. Terrorist activity may also hinder our ability to transport home heating oil if our normal means of transportation become damaged as a result of an attack. Instability in the financial markets as a result of terrorism could also affect our ability to raise capital. Terrorist activity could likely lead to increased volatility in prices for home heating oil. Insurance carriers are routinely excluding

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coverage for terrorist activities from their normal policies, but are required to offer such coverage as a result of new federal legislation. We have opted to purchase this coverage with respect to our property and casualty insurance programs. This additional coverage has resulted in additional insurance premiums.

*The impact of hurricanes and other natural disasters could cause disruptions in supply and have a material adverse effect on our business, financial condition and results of operations.*

Hurricanes, particularly in the Gulf of Mexico, and other natural disasters may cause disruptions in the supply chains for home heating oil and other petroleum products. Disruptions in supply could have a material adverse effect on our business, financial condition and results of operations, causing an increase in wholesale prices and decrease in supply.

*Cash distributions (if any) are not guaranteed and may fluctuate with performance and reserve requirements.*

Because distributions on the common units are dependent on the amount of cash generated, distributions may fluctuate based on our performance. The actual amount of cash that is available will depend upon numerous factors, including:

profitability of operations;

required principal and interest payments on debt;

debt covenants;

margin account requirements;

cost of acquisitions;

issuance of debt and equity securities;

fluctuations in working capital;

capital expenditures;

adjustments in reserves;

prevailing economic conditions;

financial, business and other factors; and

increased pension funding requirements.

Most of these factors are beyond the control of the general partner.

The partnership agreement gives the general partner discretion in establishing reserves for the proper conduct of our business. These reserves will also affect the amount of cash available for distribution.

On October 18, 2004, we announced that we would not pay a distribution on the common units. We had previously announced the suspension of distributions on the senior subordinated units on July 29, 2004. As of February 14, 2006, the amount of accrued and unpaid arrearages on the common units was \$111.0 million, or \$3.45 per common unit. Assuming that the number of outstanding common units remained at 32,165,528 and that we did not distribute any available cash from operating surplus, these arrearages would increase by \$18.5 million per quarter, or \$0.575 per common unit. If the recapitalization is not consummated, it is unlikely that regular distributions on the common units would be resumed in the foreseeable future and it is considerably less likely that regular distributions would resume on the senior subordinated units in the foreseeable future because of their subordination terms.

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### **Risks of an Investment in our Securities**

#### ***Provisions concerning change of control, default and preclusion from paying distributions in our debt instruments may affect distributions.***

Our debt instruments contain provisions relating to a change of control. As of December 31, 2005, a change of control of Star Gas Partners would require an offer to repurchase \$265 million of Star Gas Partners' senior notes at 101% of face value. After giving effect to the recapitalization, Star Gas Partners expects to have approximately \$165.0 million of its senior notes outstanding. See "Capitalization" and "Unaudited Condensed Pro Forma Financial Statements." As of the date of this prospectus, the holders of all but approximately \$5.8 million in face amount of the senior notes have waived their right to participate in a repurchase offer required to be made to senior noteholders following the recapitalization.

A change of control at the Petro level would accelerate the Petro bank debt, which was \$33.3 million as of December 31, 2005 and does not include letters of credit outstanding of \$52.9 million. However, our bank lenders have agreed that the appointment of Kestrel Heat as our new general partner shall not constitute a change of control. Further, our bank lenders have agreed to permit the heating oil segment to distribute to us funds to repurchase the minimum amount of senior notes which we are required to repurchase under our agreements with our noteholders.

These provisions continue to apply to any future transaction involving a change of control. The payments required upon a change of control under these provisions would necessarily affect our ability to make distributions to unitholders. Neither Star Gas Partners nor Petro is restricted from entering into a transaction that would trigger the change of control provisions. If these change of control provisions are triggered, some or all of the outstanding debt may become due. It is possible that Star Gas Partners or Petro would not have sufficient funds at the time of any change of control to make the required debt payments or that restrictions in its other debt instruments would not permit those payments. In some instances, lenders would have the right to foreclose on Petro's assets if debt payments were not made upon a change of control.

#### ***Restrictive covenants in the agreements governing our indebtedness and other financial obligations of Petro may reduce our operating flexibility.***

The indenture governing our senior notes and the agreement governing Petro's revolving credit facility contain various covenants that limit our ability and the ability of our subsidiaries to, among other things:

incur additional indebtedness;

make distributions to our unitholders;

purchase or redeem our outstanding equity interests or subordinated debt;

make specified investments;



create liens;

sell assets;

make acquisitions;

engage in specified transactions with affiliates;

make specified payments, loans, guarantees and transfers of assets or interests in assets;

engage in sale-leaseback transactions;

effect a merger or consolidation with or into other companies or a sale of all or substantially all of our properties or assets; and

engage in other lines of business.

These restrictions could limit our ability and the ability of Petro and its subsidiaries to obtain future financings, make needed capital expenditures, withstand a future downturn in our business or the economy in

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general or conduct operations or otherwise take advantage of business opportunities that may arise. The agreement governing Petro's revolving credit facility also requires it to maintain a fixed charge coverage ratio of 1.1 to 1.0 if availability is less than \$25 million and satisfy other financial conditions. The ability of Petro to meet this financial ratio and other conditions can be affected by events beyond its control, such as weather conditions, oil prices and general economic conditions. Accordingly, it may be unable to meet those ratios and conditions.

Any future breach of any of these covenants or Petro's failure to meet this ratio or other conditions could result in a default under the terms of the relevant indebtedness or other financial obligations, which could cause such indebtedness or other financial obligations, and by reason of cross-default provisions, the senior notes, to become immediately due and payable. If we were unable to repay those amounts, the lenders could initiate a bankruptcy proceeding or liquidation proceeding or proceed against their collateral, if any. If the lenders of Petro's indebtedness accelerate the repayment of borrowings or other amounts owed, we may not have sufficient assets to repay our indebtedness or other financial obligations.

***Unitholders have limited voting rights and do not control the general partner.***

Unitholders have no right to elect the general partner on an annual or other continuing basis. The general partner manages and operates Star Gas Partners. Unlike the holders of common stock in a corporation, unitholders have only limited voting rights on matters affecting our business. The general partner generally may not be removed unless approved by the holders of 66<sup>2</sup>/<sub>3</sub>% of the outstanding units, voting together as a single class but excluding those units held by the general partner and its affiliates. As a result, unitholders have only limited influence on matters affecting our operation, and it would be difficult for third parties to control or influence us.

***There is a limited call right that may require unitholders to sell their units at an undesirable time or price.***

If at any time less than 20% of the outstanding units of any class are held by persons other than the general partner and its affiliates, the general partner has the right to acquire all, but not less than all, of those units held by the unaffiliated persons. The price for these units will generally equal the then-current market price of the units. As a consequence, a unitholder may be required to sell his units at an undesirable time or price. The general partner may assign this acquisition right to any of its affiliates or Star Gas Partners.

***Our ability to make distributions may be adversely affected by our obligation to first reimburse the general partner.***

Before we make any distributions on the units, we will reimburse the general partner for all expenses it has incurred on our behalf. The reimbursement of those expenses and the payment of reasonable fees charged by the general partner for services could adversely affect our ability to make distributions. Reimbursable expenses and fees are determined by the general partner in its sole discretion.

***Unitholders may not have limited liability in some circumstances.***

A number of states have not clearly established limitations on the liability of limited partners for the obligations of a limited partnership. If it were determined that we had been conducting business in any state and had failed to comply with the applicable limited partnership statute, or

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that the rights or exercise of the rights by the limited partners as a group under the partnership agreement constituted participation in the control of Star Gas Partners, then a unitholder might be held liable to the same extent as the general partner for our obligations.

*Provisions in our partnership agreement may inhibit a takeover, which could adversely affect the value of our partnership securities.*

Our partnership agreement contains provisions that could delay or prevent a change in control of our management or removal of an incumbent general partner. These provisions apply even if the offer may be considered beneficial by some of our unitholders. If a change of control is delayed or prevented, the market price of our partnership securities could decline.

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### **Tax Risks to Common Unitholders**

*The increase in taxes payable by Petro in the future will reduce dividends to Star Gas Partners, which may reduce distributions to unitholders.*

Petro and its corporate affiliates do not expect to pay significant federal income tax for 2005 and 2006. However, over time the amount of federal income taxes paid by Petro and its corporate affiliates may increase. In addition, a successful Internal Revenue Service ( IRS ) challenge to the deductions of Petro, including depreciation or interest, will increase Petro's and its corporate affiliates' tax liability. This will reduce the amount of cash that Petro can distribute to us, which in turn will reduce the amount of cash that we can distribute to our unitholders. In addition, Petro and its corporate affiliates do expect to generate earnings and profits, which will make part of the distributions from these entities to Star Gas Partners taxable dividend income to the unitholders. This dividend income cannot be offset by past losses generated by our propane activities.

*Our tax treatment depends on our status as a partnership for federal income tax purposes, as well as our not being subject to entity level taxation by individual states. If the IRS were to treat us as a corporation or if we were to become subject to entity-level taxation for state tax purposes, then our cash available for distribution to you would be reduced.*

The anticipated after tax benefit of an investment in the common units depends on our being treated as a partnership for federal income tax purposes. We have not requested, and do not plan to request, a ruling from the IRS on this or any other matter affecting us.

If we were treated as a corporation for federal income tax purposes, we would pay federal income tax on our income at the corporate tax rate, which is currently a maximum of 35%. However, we would not be required to include dividends from our corporate subsidiaries in our taxable income or if we had to we would be entitled to a dividends received deduction in computing our taxable income. Distributions to you would generally be taxed again as corporate distributions, and no income, gains, losses, deductions or credits would flow through to you. Because a tax would be imposed upon us as a corporation, our cash available for distribution to you would be reduced. Thus, treatment of us as a corporation would result in a reduction in the anticipated cash flow and after tax return to you, likely causing a reduction in the value of the common units.

Current law may change, causing us to be treated as a corporation for federal income tax purposes or otherwise subjecting us to entity level taxation. For example, because of widespread state budget deficits, several states are evaluating ways to subject partnerships to entity level taxation through the imposition of state income, franchise or other forms of taxation. If any state were to impose a tax upon us as an entity, the cash available for distribution to you would be reduced. The partnership agreement provides that if a law is enacted or existing law is modified or interpreted in a manner that subjects us to taxation as a corporation or otherwise subjects us to entity level taxation for federal, state or local income tax purposes, then the minimum quarterly distribution amount and the target distribution amount will be adjusted to reflect the impact of that law on us.

*If the IRS contests the federal income tax positions we take, the market for our common units may be adversely impacted, and the costs of any contest will reduce our cash available for distribution to you.*

We have not requested any ruling from the IRS with respect to our treatment as a partnership for federal income tax purposes or any other matter affecting us. The IRS may adopt positions that differ from our counsel's conclusions expressed in this prospectus. It may be necessary to resort to

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administrative or court proceedings to sustain some or all of our counsel's conclusions or the positions we take. A court may not agree with some or all of our counsel's conclusions or the positions we take. Any contest with the IRS may materially and adversely impact the market for our common units and the price at which they trade. In addition, the costs of any contest with the IRS, because the cost will be borne indirectly by our unitholders and our general partner, will result in a reduction in cash available for distribution.

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*You may be required to pay taxes on your share of our income even if you do not receive any cash distributions from us.*

You will be required to pay federal income taxes and, in some cases, state and local income taxes on your share of our taxable income, whether or not you receive cash distributions from us. You may not receive cash distributions from us equal to your share of our taxable income or even equal to the actual tax liability that results from your share of our taxable income. Because we do not intend to pay any cash distributions to our unitholders prior to the quarter ending December 31, 2008, there is a risk that in 2006, 2007 and 2008 you will not receive cash distributions from us equal to your share of our taxable income or the tax liability that results from your share of our taxable income.

*Tax gain or loss on the disposition of our common units could be different than expected.*

If you sell your common units, you will recognize gain or loss equal to the difference between the amount realized and your tax basis in those common units. Any prior distributions to you in excess of the total net taxable income you were allocated for a common unit, which decreased your tax basis in that common unit, will, in effect, become taxable income to you if the common unit is sold at a price greater than your tax basis in that common unit, even if the price you receive is less than your original cost. A portion of the amount realized, whether or not representing gain, may be ordinary income to you.

*Tax-exempt entities, regulated investment companies and foreign persons face unique tax issues from owning common units that may result in adverse tax consequences to them.*

Investment in common units by tax-exempt entities, such as individual retirement accounts (known as IRAs), regulated investment companies (known as mutual funds), and non U.S. persons raises issues unique to them. For example, a portion of our income allocated to organizations exempt from federal income tax, including individual retirement accounts and other retirement plans, may be unrelated business taxable income and may be taxable to them. Recent legislation treats net income derived from the ownership of certain qualified publicly traded partnerships as qualifying income to a regulated investment company. However, we do not expect to be a qualified publicly traded partnership for this purpose. Accordingly, some of our income may not be qualifying income to a regulated investment company. We will withhold tax at a rate of 30% on the portion of our dividend and interest income that is allocable to non U.S. persons. Moreover, if we realize other income that is effectively connected with a U.S. trade or business, distributions to non U.S. persons will be reduced by withholding taxes at the highest applicable effective tax rate, and non U.S. persons will be required to file U.S. federal income tax returns and pay tax on their share of our taxable income.

*The sale or exchange of 50% or more of our capital and profits interests will result in the termination of our partnership for federal income tax purposes.*

We will be considered to have terminated for federal income tax purposes if there is a sale or exchange of 50% or more of the total interests in our capital and profits within a 12 month period. Our termination would, among other things, result in the closing of our taxable year for all unitholders. Please read [Material Tax Consequences](#) [Disposition of Common Units](#) [Constructive Termination](#) for a discussion of the consequences of our termination for federal income tax purposes.

*The issuance of units in the recapitalization will likely result in an ownership change of our corporate subsidiary, Star/Petro, under the Tax Code and as a result, Star/Petro will be materially restricted in its ability to use its net operating loss carryforwards to reduce its future taxable income.*

We believe that the issuance of units in the recapitalization will likely result in an ownership change of our corporate subsidiary, Star/Petro, under the Tax Code. As a result of this ownership change, Star/Petro will be materially restricted in its ability to use its net operating loss carryforwards to reduce its future taxable income.

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As of December 31, 2005, Star Petro had a federal net operating loss carryover of approximately \$166.4 million. These net operating loss carryforwards (prior to an ownership change ) will begin to expire in 2025 and are generally available to reduce future taxable income that would otherwise be subject to federal income taxes.

As a result of the ownership change, Star/Petro will be restricted annually in its ability to use its net operating loss carryforwards to reduce its federal taxable income. We believe that the restriction may entirely eliminate Star/Petro's ability to use its net operating loss carryforwards. The restriction on Star/Petro's ability to use net operating loss carryforwards to reduce its federal tax liability will reduce the amount of cash Star/Petro has available to make distributions to us. Consequently, the restriction will reduce the amount of cash we have available to distribute to our unitholders.



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**USE OF PROCEEDS**

We will receive approximately \$39.375 million of proceeds before deducting any expenses from the rights offering (assuming full unitholder participation). These recapitalization expenses are estimated to be \$6.5 million. We plan to use the net proceeds we receive from the rights offering, together with \$16.875 million in proceeds from the issuance of an aggregate of 6,750,000 common units to Kestrel Heat and M2, and additional funds from operations, to repurchase at least \$60 million and, at our option, up to approximately \$73.1 million in face amount of our senior notes (assuming full noteholder participation in the senior notes tender offer). Any additional proceeds that we receive in connection with the exercise of M2's standby commitment at \$2.25 per unit will reduce the amount of funds from operations that are needed to repurchase senior notes. The senior notes bear interest at a rate of 10.25% per annum and mature on February 15, 2013.

**Table of Contents****CAPITALIZATION**

The following table sets forth our historical capitalization as of December 31, 2005 on an actual basis and as adjusted to give pro forma effect to the following elements of the recapitalization (see Unaudited Condensed Pro Forma Financial Information):

the issuance of 6,750,000 common units to Kestrel Heat and M2 for a purchase price of \$2.50 per unit and the issuance to Kestrel Heat of 325,729 general partner units;

the issuance of 19,687,500 common units in the rights offering at an exercise price of \$2.00 per unit;

the use of the net proceeds from the issuance of common units to Kestrel Heat and M2 and the rights offering, together with additional cash from operations, to repurchase approximately \$73.1 million of senior notes (assuming full noteholder participation in the senior notes tender offer); as of the date of this prospectus, the holders of an aggregate of approximately \$5.8 million in senior notes have not yet agreed to tender their notes in the tender offer; the principal amount of any senior notes, plus any interest and premium payments that we are required to make in respect of senior notes tendered for repurchase in the change of control repurchase offer, will reduce on a dollar-for-dollar basis the amount of senior notes that we shall repurchase for cash in connection with the closing of the recapitalization;

the conversion of approximately \$26.9 million of senior notes into 13,433,962 (subject to adjustment for rounding) newly issued common units;

the conversion of each senior subordinated unit and each junior subordinated unit into one common unit;

the write-off of net deferred charges and debt premium of \$1.4 million; and

the estimated expenses of the recapitalization of \$6.5 million.

	As of	
	December 31, 2005	
	(in thousands)	
	Actual	Pro Forma
Cash and cash equivalents	\$ 9,217	\$ 9,217
Debt		
<b>Star Gas:</b>		
10.25% Senior Notes due 2013	\$ 267,244	\$ 166,397
<b>Heating Oil Segment:</b>		
Revolving Credit Facility (b)	33,251	58,004(a)(c)
Acquisition Notes Payable	183	183
Subordinated Debentures	666	666

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Total debt	\$ 301,344	\$ 225,250
Less: Revolving Credit Facility	(33,251)	(58,004)
Current Portion of Acquisition Notes and Subordinated Debentures	(754)	(754)
Total long-term debt	\$ 267,339	\$ 166,492
Total partner s capital	116,767	192,362
Total capitalization	\$ 384,106	\$ 358,854

- 
- (a) Reflects the repayment of approximately \$73.1 million in face amount of our senior notes (assuming full noteholder participation in the senior notes tender offer). Pursuant to the tender offer for the senior notes, Star Gas Partners must exchange for cash at least \$60 million of senior notes but not more than \$73.1 million. Star Gas Partners intends to offer to repurchase approximately \$73.1 million of senior notes, subject to cash availability at the time of closing. If Star Gas Partners tenders for \$60.0 million of senior notes, the

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increase in working capital borrowings would be \$11.1 million and long-term debt will decrease by \$87.6 million. As of the date of this prospectus, the holders of approximately \$5.8 million in face amount of senior notes had not yet agreed to exchange their notes in the tender offer. If all of these noteholders do not participate in the tender offer and do not tender their notes in connection with the subsequent change of control repurchase offer, the amount of senior notes that we would repurchase for cash in connection with the recapitalization would be at least approximately \$54.1 million but not more than approximately \$67.2 million. If all of our common unitholders do not participate in the rights offering and M2 purchases all of the common units pursuant to its standby commitment and we offer to repurchase \$73.1 million of our senior notes, the increase in working capital borrowings would be \$19.8 million. If we tender for \$60 million of senior notes and common unitholders do not participate in the rights offering, the increase in working capital borrowings would be \$6.2 million and long-term debt will decrease by \$87.6 million.

- (b) The heating oil segment's revolving credit facility currently includes a \$260 million revolving loan facility (which increases to \$310 million during the peak heating season from December 1 through March 31), subject to borrowing base requirements and coverage ratios, of which up to \$75 million may be used to issue letters of credit. This facility contains various restrictive and affirmative covenants. The most restrictive of these covenants relate to the incurrence of additional indebtedness, and restrictions on dividends, certain investments, guarantees, loans, sales of assets and other transactions.
- (c) Assumes full unitholder participation in the rights offering at an exercise price of \$2.00 per unit. Any additional proceeds that we receive in connection with the exercise of M2's standby commitment at \$2.25 per unit will reduce the amount of funds from operations that are needed to repurchase senior notes by \$4.9 million.

**Table of Contents****UNIT OWNERSHIP**

The following table shows the approximate number of units outstanding before and after the proposed recapitalization.

	<b>Before Recapitalization*</b>		<b>After Recapitalization</b>	
	<b>Number</b>	<b>Percentage</b>	<b>Number</b>	<b>Percentage</b>
<b>Common Units</b>				
Existing common units	32,165,528	88.8%	32,165,528	42.3%
Issued to Kestrel entities**			6,750,000	8.9%
Issued in rights offering			19,687,500	25.9%
Issued to senior noteholders			13,433,962	17.6%
Issued to subordinated unitholders			3,737,346	4.9%
Subtotal	32,165,528	88.8%	75,774,336	99.6%
<b>Subordinated Units</b>				
Senior subordinated units	3,391,982	9.4%		
Junior subordinated units	345,364	0.9%		
Subtotal	3,737,346	10.3%		
<b>General Partner Units</b>	325,729	0.9%	325,729	0.4%
<b>Total</b>	<b>36,228,603</b>	<b>100%</b>	<b>76,100,065</b>	<b>100%</b>

\* As of April 5, 2006.

\*\* Assumes no additional units are acquired in this rights offering by M2 pursuant to its standby commitment.

**Table of Contents****PRICE RANGE OF COMMON UNITS AND CASH DISTRIBUTIONS**

The common units are listed and traded on the New York Stock Exchange under the symbol SGU. The following table shows the high and low closing prices for the common units on the NYSE and the cash distribution paid per common unit for the quarterly periods indicated.

	Price Range Per Common Unit		Cash
	High	Low	Distributions(1)
<b>Fiscal 2004</b>			
December 31,	\$ 24.93	21.79	0.575
March 31,	25.59	22.85	0.575
June 30,	25.53	20.00	0.575
September 30,	24.25	20.54	0.575
<b>Fiscal 2005</b>			
December 31,	\$ 22.23	4.32	0.0
March 31,	7.22	3.11	0.0
June 30,	4.11	1.94	0.0
September 30,	3.64	2.39	0.0
<b>Fiscal 2006</b>			
December 31,	\$ 2.39	\$ 1.05	0.0
March 31,	2.97	1.84	0.0
June 30,	2.77(2)	2.61(2)	0.0

- (1) Distributions are shown in the quarter in which they were paid.  
(2) Through April 5, 2006.

On December 2, 2005, the last trading day prior to our public announcement of the recapitalization transaction, the closing sales price per common unit was \$1.32. On April 5, 2006, the last trading day prior to the date of this prospectus, the closing sales price of the common units was \$2.61. Unitholders are urged to obtain a current quotation for the common units. In addition, on April 5, 2006, there were 32,165,528 common units outstanding and approximately 555 holders of record of Star Gas Partners' common units.

On October 18, 2004, we announced that we would not pay a distribution on the common units. We had previously announced the suspension of distributions on the senior subordinated units (and junior subordinated units and general partner units) on July 29, 2004. As of February 14, 2006, the amount of unpaid arrearages on the common units was \$111.0 million, or \$3.45 per common unit. Assuming that the number of outstanding common units remained at 32,165,528 and that we did not distribute any available cash from operating surplus, these arrearages would increase by \$18.5 million per quarter, or \$0.575 per common unit. If the recapitalization is not consummated, it is unlikely that regular distributions on the common units would be resumed in the foreseeable future and it is considerably less likely that regular distributions would resume on the senior subordinated units in the foreseeable future because of their subordination terms.

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**THE RIGHTS OFFERING**

**General**

As soon as practicable after 5:00 p.m., New York City time, on April 7, 2006, which is the commencement date for the rights offering, we are distributing to each holder of our common units, at no charge, a .6121 non-transferable subscription right for each common unit owned by such holder. The rights will be evidenced by rights certificates. Only our common unitholders of record as of the record date, April 6, 2006, will receive subscription rights.

Each full subscription right entitles its holder to purchase one common unit representing a limited partnership interest at the subscription price of \$2.00 per unit. We will not issue fractional units or pay cash in lieu thereof. Instead, we will round the total number of units each rightsholder is entitled to purchase upward to the nearest whole unit.

The following describes the rights offering in general and assumes (unless specifically provided otherwise) that you are a record holder of our common units. If you hold your units in a brokerage account or through a dealer or other nominee, please see the information included below under the heading **Beneficial Owners**. As used in this prospectus, the term **business day** means any day on which securities may be traded on The New York Stock Exchange.

**Reasons for the Rights Offering**

The rights offering is one of the principal elements of a recapitalization of Star Gas Partners. We intend to use the \$56.25 million in new equity financing that we will generate in connection with the financial restructuring, together with additional funds from operations, to repurchase up to approximately \$73.1 million in face amount of senior notes (assuming full noteholder participation). As of the date of this prospectus, the holders of an aggregate of approximately \$5.8 million in senior notes have not yet agreed to tender their notes in the tender offer. The principal amount of any senior notes, plus any interest and premium payments that we are required to make in respect of senior notes tendered for repurchase in the change of control repurchase offer, will reduce on a dollar-for-dollar basis the amount of senior notes that we shall repurchase for cash in connection with the closing of the recapitalization. In addition, we have agreed to permit the holders of senior notes to convert \$26.9 million in face amount of such notes into 13,433,962 (subject to adjustment based on rounding) new common units at an exchange price of \$2.00 per unit in connection with the closing of the transaction.

**Determination of Subscription Price**

The subscription price was determined pursuant to the unit purchase agreement with the Kestrel entities. The subscription price of our common units may not reflect the value of our partnership or our common units, the book value of our assets, historical or future cash flows, financial condition, recent or historical unit prices or any other established criteria for valuation. We cannot assure you that our common units will trade at prices equal to or in excess of the subscription price at any time after the date of this prospectus or the consummation of the recapitalization.

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At December 2, 2005, the last trading day prior to our public announcement of the recapitalization transaction, the closing sales price of the common units was \$1.32. On April 5, 2006, the last trading day prior to the date of this prospectus, the closing sales price per common unit was \$2.61.

### **No Fractional Units**

We will not issue or pay cash in lieu of fractional units. Instead, we will round the number of units each rightsholder is entitled to acquire upward to the nearest whole unit based on the total number of units to which



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such rightsholder subscribes. For example, if you own 100 common units and exercise your subscription privilege with respect to all those units, you will receive 62 common units, instead of the 61.21 common units you would have received without rounding.

## **Expiration Time**

You may exercise the subscription privilege at any time before the Expiration Time, which is 5:00 p.m., New York City time, on April 25, 2006, or such later date and time to which the rights offering is extended. If you do not exercise your rights before the Expiration Time, then your rights will expire and become null and void. Accordingly, if a rightsholder desires to exercise its subscription rights, the subscription agent must actually receive all required documents and payments for that rightsholder before that date and time. We will not be obligated to honor your exercise of rights if the subscription agent receives any of the required documents relating to your exercise of subscription privileges after the Expiration Time, regardless of when you transmitted the documents, except if you have timely transmitted the documents pursuant to the guaranteed delivery procedures described below.

We may extend the Expiration Time for any reason; however, you will NOT be able to revoke your exercise of subscriptions. If we elect to extend the date the rights expire, we will issue a press release announcing the extension before 9:00 a.m. on the first business day after the most recently announced Expiration Time.

## **Subscription Privileges**

Your rights entitle you to a subscription privilege. Under the subscription privilege, each full right entitles the holder to purchase one common unit upon delivery of the required documents and payment of the subscription price per unit, prior to the Expiration Time. Any unitholder who chooses not to exercise its rights will experience dilution to its equity interest in our partnership. Even those unitholders who exercise their rights will experience dilution as a result of the issuance of approximately 43,608,808 new common units in connection with the recapitalization. No rightsholder will have the right to oversubscribe.

## **Non-Transferability of Rights**

Except in the limited circumstances described below, rights are non-transferable and non-assignable. Only you may exercise your rights. Notwithstanding the foregoing, your rights may be transferred by will or by the laws of descent and distribution of the state of your domicile at the time of your death. If the rights are transferred as permitted, we must receive evidence that is satisfactory to us that the transfer was proper, prior to the Expiration Time.

## **Exercising Your Rights**

You may exercise your rights by delivering the following to the subscription agent before the Expiration Time:

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your properly completed and executed rights certificate (which is included herewith) evidencing the exercised rights with any required signature guarantees or other supplemental documentation; and

your payment in full of the subscription price for each unit subscribed for pursuant to the subscription privilege.

Alternatively, if you deliver a notice of guaranteed delivery together with your subscription price payment for units prior to the Expiration Time, you must deliver the rights certificate within three business days after the date the notice of guaranteed delivery is received by the subscription agent using the guaranteed delivery procedures described below under the heading **Guaranteed Delivery Procedures**.

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### **Payment of Subscription Price**

Your cash payment of the subscription price for the common units must be made by either certified check or bank draft drawn upon a U.S. bank payable to LaSalle Bank National Association or by wire transfer of immediately available funds to the account maintained by LaSalle Bank National Association for the purpose of accepting subscriptions under this offering, as more fully described in the document entitled "Instructions for Use of Star Gas Partners, L.P. Common Unit Right Certificates." You should send your rights certificate and payment for common units subscribed for and any other required documentation to the subscription agent as set forth below under "Delivery of Subscription Materials and Payment."

We will retain any interest earned on any cash funds held by the subscription agent or by us in connection with the rights offering prior to the consummation of the rights offering or the return of such funds, if required, pursuant to this prospectus.

The subscription agent will hold your payment of the subscription price for the rights in a segregated account with other payments received from holders of rights until we issue your units.

We will not charge a fee to holders for exercising their rights. However, any holder exercising its rights through a broker, dealer or nominee will be responsible for any fees charged by its broker, dealer or nominee.

### **Exercising a Portion of Your Rights**

You may subscribe for fewer than all of the common units that you are eligible to purchase pursuant to the subscription privilege represented by your rights certificate; however, once the rights offering expires, you will no longer be entitled to subscribe for common units.

### **Calculation of Rights Exercised**

If you do not indicate the number of common units being purchased for the subscription rights you receive, or do not forward full payment of the aggregate subscription price for the number of common units that you indicate are being purchased, then you will be deemed to have exercised the subscription privilege with respect to the maximum number of units that may be purchased for the aggregate subscription price payment you delivered to the subscription agent. If your aggregate subscription price payment is greater than the amount you owe for your subscription, you will be deemed to have exercised the full subscription privilege to purchase the maximum number of common units available to you pursuant to your subscription privilege and the excess amount will be returned to you by mail or similarly prompt means, without interest or deduction as soon as practicable after the Expiration Time.

### **Instructions For Completing the Rights Certificates**

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You should read and follow the instructions accompanying the rights certificates carefully. If you want to exercise your rights, you must send your completed rights certificates, any necessary accompanying documents and payment of the subscription price to the subscription agent. **You should not send the rights certificates, any related documentation or payment of the subscription price to us.** Any rights certificates and other items received by us relating to subscriptions will be returned to the sender.

You bear all risk for the method of delivery of rights certificates, any necessary accompanying documents and payment of the subscription price to the subscription agent. If you send the rights certificates and other items by mail, we recommend that you send them by registered mail, properly insured, with return receipt requested. You should allow a sufficient number of days to ensure delivery and clearance of cash payment prior to the Expiration Time.

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**Signature Guarantee May Be Required**

Your signature on each rights certificate must be guaranteed by an eligible institution such as a member firm of a registered national securities exchange, a member of the National Association of Securities Dealers, Inc. or a commercial bank or trust company having an office or correspondent in the United States, subject to standards and procedures adopted by the subscription agent, unless:

your rights certificate is registered in your name; or

you are an eligible institution.

**Delivery of Subscription Materials and Payment**

You should deliver your rights certificate and payment for common units subscribed for, as well as any nominee holder certifications, notices of guaranteed delivery, Depository Trust Company participant subscription forms and any other required documentation to the subscription agent, LaSalle Bank National Association, as follows:

*By Mail:*

LaSalle Bank National Association  
135 S. LaSalle Street, Suite 1811  
Chicago, Illinois 60603  
Telephone: (800) 246-5761, Menu Option 2  
Facsimile: (312) 904-2079  
Attention: Corporate Trust Operations

*By Hand:*

LaSalle Bank National Association  
135 S. LaSalle Street, Suite 1811  
Chicago, Illinois 60603  
Telephone: (312) 904-5091  
Facsimile: (312) 904-2079  
Attention: Joseph Pellicore

*By Overnight Courier:*

LaSalle Bank National Association  
135 S. LaSalle Street, Suite 1811  
Chicago, Illinois 60603  
Telephone: (800) 246-5761, Menu Option 2  
Facsimile: (312) 904-2079  
Attention: Corporate Trust Operations

**Guaranteed Delivery Procedures**

If you wish to exercise your rights, but you do not have sufficient time to deliver the rights certificate evidencing your rights to the subscription agent before the Expiration Time, you may exercise your rights by the following guaranteed delivery procedures:

provide your payment in full of the subscription price for each common unit being subscribed for pursuant to the subscription privilege to the subscription agent before the Expiration Time;

deliver a notice of guaranteed delivery to the subscription agent at or before the Expiration Time; and

deliver the properly completed rights certificate evidencing the rights being exercised (and, if applicable for a nominee holder, the related nominee holder certification), with any required signatures guaranteed, to the subscription agent, within three business days following the date the notice of guaranteed delivery was received by the subscription agent.

Your notice of guaranteed delivery must be substantially in the form provided with the Instructions For Use of Star Gas Partners, L.P. Common Units Rights Certificates distributed to you with your rights certificate.

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Your notice of guaranteed delivery must come from an eligible institution which is a member of, or a participant in, a signature guarantee program acceptable to the subscription agent. In your notice of guaranteed delivery you must state:

your name;

the number of rights represented by your rights certificate, the number of common units you are subscribing for pursuant to the subscription privilege; and

your guarantee that you will deliver to the subscription agent any rights certificates evidencing the rights you are exercising within three business days following the date the subscription agent receives your notice of guaranteed delivery.

You may deliver the notice of guaranteed delivery to the subscription agent in the same manner as the rights certificate at the addresses set forth under **Delivery of Subscription Materials and Payment** above.

You may also transmit the notice of guaranteed delivery to the subscription agent by facsimile transmission to (312) 904-2079. To confirm facsimile deliveries, you may call (800) 246-5761, Menu Option 2.

The information agent will send you additional copies of the form of notice of guaranteed delivery if you need them. Please call the information agent, Georgeson Shareholder, at (888) 877-5392.

## **Notice To Nominees**

If you are a broker, a dealer, a trustee or a depository for securities who holds our common units for the account of others as a nominee holder, you should notify the respective beneficial owners of those units of the issuance of the rights as soon as possible to find out the beneficial owners' intentions. You should obtain instructions from the beneficial owner with respect to the rights, as set forth in the instructions we have provided to you for your distribution to beneficial owners. If the beneficial owner so instructs, you should complete the appropriate rights certificates and the related nominee holder certification and submit them to the subscription agent with the proper payment. A nominee holder that holds units for the account(s) of more than one beneficial owner may exercise the number of rights to which all such beneficial owners in the aggregate otherwise would have been entitled if they had been direct record holders of units on the record date, so long as the nominee submits the appropriate rights certificates and certifications and proper payment to the subscription agent.

## **Beneficial Owners**

If you are a beneficial owner of common units or rights that you hold through a nominee holder, we will ask your broker, dealer or other nominee to notify you of this rights offering. If you wish to exercise your rights, you will need to have your broker, dealer or other nominee act for you. To indicate your decision with respect to your rights, you should complete and return to your broker, dealer or other nominee the form entitled **Beneficial Owners Election Form**. You should receive this form from your broker, dealer or other nominee with the other subscription materials.

**Procedures For DTC Participants**

We expect that your exercise of your subscription privilege with respect to rights may be made through the facilities of DTC. If you exercise your subscription privilege with respect to rights through DTC we refer to your rights as DTC Exercised Rights. Please call the information agent, Georgeson Shareholder, at (888) 877-5392 to obtain copies of the DTC participant exercise form and the nominee holder certification.

**Determinations Regarding the Exercise of Rights**

We will decide all questions concerning the timeliness, validity, form and eligibility of your exercise of rights. Our decisions will be final and binding. We, in our sole discretion, may waive any defect or irregularity,



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or permit a defect or irregularity to be corrected within whatever time we determine. We may reject the exercise of any of your rights because of any defect or irregularity. Your subscription will not be deemed to have been received or accepted until all irregularities have been waived by us or cured by you within the time we decide, in our sole discretion.

We reserve the right to reject your exercise of rights if your exercise is not in accordance with the terms of the rights offering or in proper form. Neither we nor our general partner, nor its members, officers or directors or the subscription agent will have any duty to notify you of a defect or irregularity in your exercise of the rights. We will not be liable for failing to give you that notice. We also will not accept your exercise of rights if our issuance of common units pursuant to your exercise could be deemed unlawful or materially burdensome. See **Regulatory Limitation** and **Compliance with State Regulations Pertaining to the Rights Offering** below.

## **No Revocation of Exercised Rights**

Once you have exercised your subscription privilege, you may NOT revoke your exercise. Even if we extend the Expiration Time, you may not revoke your exercise.

## **Subscription Agent**

We have appointed LaSalle Bank National Association as subscription agent for the rights offering. We will pay its fees and expenses related to the rights offering.

## **Information Agent**

With respect to rights, you may direct any questions or requests for assistance concerning the method of exercising your rights, additional copies of this prospectus, the instructions for the rights, the nominee holder certification, the notice of guaranteed delivery or other subscription materials referred to herein, to the information agent for the rights offering, at the following telephone number and address:

Georgeson Shareholder

17 State Street

New York, NY 10004

Telephone: (888) 877-5392

## **No Recommendations to Rightsholders**

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Neither we nor the board of directors of our general partner has made any recommendation as to whether you should exercise your rights. You should decide whether to subscribe for common units or simply take no action with respect to your rights, based upon your own assessment of your best interests. We have not yet received indications from any unitholders that they will exercise their rights. M2, a Kestrel affiliate, has agreed to provide a standby commitment to purchase all of the common units which are not purchased pursuant to this rights offering. In addition, members of the board of directors of our general partner and our senior management who own an aggregate of 35,125 common units have not yet indicated whether they intend to exercise their rights. See Risk Factors, Information Regarding Kestrel Heat Interests of the Proposed Executive Officers and Directors in the Recapitalization and Conflicts of Interest.

### **Conditions of the Rights Offering**

The consummation of the rights offering is conditioned upon the simultaneous closing of the proposed recapitalization of Star Gas Partners pursuant to the Kestrel unit purchase agreement.

### **Rejection of Rights**

We reserve the right to reject your exercise of rights if we determine that your exercise is not in proper form or otherwise not in accordance with the terms of this rights offering. Neither we nor the subscription agent will

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have any duty to notify you of a defect or irregularity in your exercise of rights. We will not be liable for failing to give you that notice. We will also not accept your exercise of rights if our issuance of common units pursuant to your exercise could be deemed unlawful or materially burdensome. In addition, we will not be required to accept subscriptions or issue units until after the Expiration Time.

## **Termination**

The consummation of the rights offering is conditioned upon the simultaneous closing of the proposed recapitalization of Star Gas Partners. In addition, we may terminate the rights offering for any reason at any time before the Expiration Time. If we terminate the rights offering, we will promptly issue a press release announcing the termination, and we will promptly thereafter return all subscription payments. We will not be obligated to issue units to rightsholders that have exercised their right prior to the termination of the rights offer. We will not pay interest on, or deduct any amounts from, subscription payments if we terminate the rights offering.

## **Foreign Unitholders**

We will not mail rights certificates to unitholders on the record date or to subsequent transferees whose addresses are outside the United States. Instead, the subscription agent will hold the rights certificates for those holders' accounts. To exercise their rights, foreign holders must notify the subscription agent before 11:00 a.m., New York City time, on April 20, 2006, three business days prior to the Expiration Time, and must establish to the satisfaction of the subscription agent that such exercise is permitted under applicable law.

## **Regulatory Limitation**

We will not be required to issue to you common units pursuant to the rights offering if, in our opinion, you would be required to obtain prior clearance or approval from any state or federal regulatory authorities to own or control such units and if, at the Expiration Time, you have not obtained such clearance or approval.

## **Issuance of Common Units**

Unless we earlier terminate the rights offering, the subscription agent will issue to you the common units purchased by you in the rights offering as soon as practicable after the Expiration Time. Each subscribing holder's new common units will be issued in the same form, certificated or book-entry, as the rights exercised by that holder. Common units that you purchase in the rights offering will be listed on the New York Stock Exchange.

Your payment of the aggregate subscription price for common units will be retained by the subscription agent and will not be delivered to us, unless and until your subscription is accepted and you are issued your unit certificates. We will not pay you any interest on funds paid to the subscription agent, regardless of whether the funds are applied to the subscription price or returned to you. You will have no rights as a unitholder of our company with respect to the subscribed for common units until the certificates representing such units are issued to you or the units are deposited in the book-entry account held on your behalf. Upon our issuance of the certificates or the deposit of the units in the

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applicable book-entry account, you will be deemed the owner of the units you purchased by exercise of your rights. Unless otherwise instructed in the rights certificates, the units issued to you pursuant to your subscription will be registered in your name or the name of your nominee, if applicable.

We will not issue any fractional units. Instead, we will round the number of units each rightsholder is entitled to acquire upward to the nearest whole share.

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### **Units Outstanding**

As of December 31, 2005, we had outstanding a total of 32,165,528 common units, 3,391,982 senior subordinated units, 345,364 junior subordinated units and 325,729 general partner units. Following completion of the rights offering, the number of outstanding common units will increase by 19,687,500 common units, as a result of the issuance of all common units purchased in the rights offering or sold to M2 pursuant to its standby commitment. In addition, we will issue an aggregate of 6,750,000 common units to Kestrel Heat and M2, 13,433,962 (subject to adjustment based on rounding) newly issued common units to our senior noteholders upon the exchange of approximately \$26.9 million in face amount of senior notes and 3,737,346 common units upon conversion of the senior subordinated units and junior subordinated units in connection with the recapitalization, for a total number of common units outstanding equal to approximately 75,774,336.

### **Compliance With Regulations Pertaining to the Rights Offering**

We are not making the rights offering in any state or other jurisdiction in which it is unlawful to do so. We will not sell or accept an offer to purchase common units from you if you are a resident of any state or other jurisdiction in which the sale or offer of the rights would be unlawful. We may delay the commencement of the rights offering in certain states or other jurisdictions in order to comply with the laws of those states or other jurisdictions. However, we may decide, in our sole discretion, not to modify the terms of the rights offering as may be requested by certain states or other jurisdictions. If that happens and you are a resident of the state or jurisdiction that requests the modification, you will not be eligible to participate in the rights offering. We do not expect that there will be any changes in the terms of the rights offering.

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**PLAN OF DISTRIBUTION**

We are making this rights offering directly to you, the holders of our common units on a pro rata basis for each common unit held at the close of business on April 6, 2006, the record date for this rights offering.

We will pay Georgeson Shareholder, the information agent, a fee of approximately \$7,500.00 and LaSalle Bank National Association, the subscription agent with respect to the rights, a fee of approximately \$10,000.00 for their services in connection with this rights offering (which includes the subscription agent's fees associated with the exercise of rights). We have also agreed to reimburse the information agent and the subscription agent their reasonable expenses and to indemnify them against certain liabilities.

We estimate that our total expenses in connection with the recapitalization, including registration, legal and accounting fees, will be approximately \$6.5 million.

We have not employed any brokers, dealers or underwriters in connection with the solicitation or exercise of rights. Except as described in this section, we are not paying any other commissions, fees or discounts in connection with the rights offering. Some of our employees may solicit responses from you as a holder of rights, but we will not pay our employees any commissions or compensation for such services other than their normal employment compensation.

**Table of Contents****INFORMATION REGARDING KESTREL HEAT**

The recapitalization would result in Kestrel Heat replacing Star Gas as our general partner. Kestrel Heat is a Delaware limited liability company that was formed on November 29, 2005 for the purpose of performing the duties of the general partner of Star Gas Partners. Kestrel Heat is wholly owned by Kestrel. Kestrel is a private equity investment partnership firm formed by Yorktown, Paul A. Vermynen, Jr. and other investors.

**Proposed Directors and Executive Officers of Kestrel Heat**

The following table sets forth the names, ages and positions of the individuals proposed to be designated as executive officers and directors of Kestrel Heat if the recapitalization is consummated. Additionally, if the recapitalization is consummated, Kestrel Heat intends to elect up to two additional directors who meet the independence requirements under applicable SEC and NYSE regulations for service on an audit committee. William P. Nicoletti currently serves as an independent director and a member of the audit committee of Star Gas.

<u>Name</u>	<u>Age</u>	<u>Position</u>
Joseph P. Cavanaugh	68	Chief Executive Officer and Director
Daniel P. Donovan	59	President, Chief Operating Officer and Director
Richard F. Ambury	49	Chief Financial Officer
Paul A. Vermynen, Jr.	59	Chairman, Director
Bryan H. Lawrence	62	Director
Sheldon B. Lubar	75	Director
William P. Nicoletti	60	Director

**Joseph P. Cavanaugh.** Mr. Cavanaugh has been Chief Executive Officer and a director of Star Gas LLC since March 2005. From December 2004, after the sale of Star Gas Partners propane segment to Inergy L.P. to March 2005, Mr. Cavanaugh was employed by Inergy to direct the transition of the business to them. From March 1999 to December 2004 Mr. Cavanaugh was Chief Executive Officer of Star Gas Partners propane segment. From December 1997 to March 1999, Mr. Cavanaugh served as President and Chief Executive Officer of Star Gas Corporation, the predecessor general partner. From October 1979 to December 1997, Mr. Cavanaugh held various financial and management positions with Petro. Mr. Cavanaugh is a graduate of Iona College and has an MS from Pace University.

**Daniel P. Donovan.** Mr. Donovan has been President of Star Gas Partners heating oil segment since May 2004 and President and Chief Operating Officer of Star Gas LLC since March 2005. From January 1980 to May 2004, he held various management positions with Meenan Oil, including Vice President and General Manager from 1998 to 2004. Mr. Donovan worked for Mobil Oil Corp. from 1971 to 1980. His last position with Mobil was President and General Manager of its heating oil subsidiary in New York City and Long Island. Mr. Donovan is a graduate of St. Francis College in Brooklyn, New York and also has an M.B.A. from Iona College.

**Richard F. Ambury.** Mr. Ambury has been Chief Financial Officer, Treasurer and Secretary of Star Gas LLC since May 2005. From November 2001 to May 2005, Mr. Ambury was Vice President and Treasurer of Star Gas LLC. From March 1999 to November 2001, Mr. Ambury was Vice President of Star Gas Propane, L.P. From February 1996 to March 1999, Mr. Ambury served as Vice President Finance of Star Gas Corporation, the predecessor general partner. Mr. Ambury was employed by Petro from June 1983 through February 1996, where he served in various accounting/finance capacities. From 1979 to 1983, Mr. Ambury was employed by a predecessor firm of KPMG, a public accounting firm. Mr. Ambury has been a Certified Public Accountant since 1981 and is a graduate of Marist College.

**Paul A. Vermylen, Jr.** Mr. Vermylen is a founder and serves as President of Kestrel. Mr. Vermylen has been employed since 1971, serving in various capacities, including as a Vice President of Citibank N.A. and Vice President-Finance of Commonwealth Oil Refining Co. Inc. Mr. Vermylen served as Chief Financial Officer of



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Meenan Oil Co., L.P. from 1982 until 1992 and as President of Meenan Oil Co., L.P. until 2001, when Meenan was acquired by Star Gas Partners, L.P. Since 2001, Mr. Vermynen has pursued private investment opportunities. Mr. Vermynen is a director of Thermal Ventures II, LP, and he also serves as a director of certain non-public companies in the energy industry in which Kestrel holds equity interests including Downeast LNG, Inc. and COALition Energy, LLC. Mr. Vermynen is a graduate of Georgetown University, and also has a M.B.A. from Columbia University.

**Bryan H. Lawrence.** Mr. Lawrence is a founder and senior manager of Yorktown Partners LLC, the manager of the Yorktown group of investment partnerships, which make investments in companies engaged in the energy industry. The Yorktown partnerships were formerly affiliated with the investment firm of Dillon, Read & Co. Inc., where Mr. Lawrence had been employed since 1966, serving as a Managing Director until the merger of Dillon Read with SBC Warburg in September 1997. Mr. Lawrence also serves as a director of Crosstex Energy, Inc., D&K Healthcare Resources, Inc., Hallador Petroleum Company, TransMontaigne Inc. (each a United States publicly traded company) and certain non-public companies in the energy industry in which Yorktown partnerships hold equity interests including PetroSantander Inc., Savoy Energy, L.P., Athanor Resources Inc., Camden Resources, Inc., ESI Energy Services Inc., Ellora Energy Inc., and Dernick Resources Inc. Mr. Lawrence also serves as a director of Crosstex Energy GP, LLC, the general partner of Crosstex Energy, L.P. (a United States publicly traded company). Mr. Lawrence is a graduate of Hamilton College and also has an M.B.A. from Columbia University.

**Sheldon B. Lubar.** Mr. Lubar has been Chairman of the board of Lubar & Co. Incorporated, a private investment and venture capital firm he founded, since 1977. He was Chairman of the board of Christiana Companies, Inc., a logistics and manufacturing company, from 1987 until its merger with Weatherford International in 1995. Mr. Lubar had also been Chairman of Total Logistics, Inc., a logistics and manufacturing company until its acquisition in 2005 by SuperValu Inc. He serves as a director of Grant Prideco, Inc., an energy services company, since 2000; and Weatherford International, Inc., an energy services company, since 1995; a director of Crosstex Energy, Inc. since January 2004 and Crosstex Energy GP, LLC, the General Partner of Crosstex Energy, L.P. He is also a Director of several private companies. Mr. Lubar holds a bachelor's degree in Business Administration and a Law degree from the University of Wisconsin-Madison. He was awarded an honorary Doctor of Commercial Science degree from the University of Wisconsin-Milwaukee.

**William P. Nicoletti.** Mr. Nicoletti has been Non-Executive Chairman of the board of Star Gas LLC since March 2005. Mr. Nicoletti has been a Director of Star Gas LLC since March 1999 and was a Director of Star Gas Corporation, the predecessor general partner from November 1995 until March 1999. He is Managing Director of Nicoletti & Company, Inc., a private investment banking firm. Mr. Nicoletti was formerly a senior officer and head of Energy Investment Banking for E. F. Hutton & Company, Inc., PaineWebber Incorporated and McDonald Investments, Inc. Mr. Nicoletti is a director of MarkWest Energy Partners, L.P. and SPI Petroleum, LLC. Mr. Nicoletti is a graduate of Seton Hall University and also has an M.B.A. from Columbia University.

## **Interests of the Proposed Executive Officers and Directors in the Recapitalization**

Kestrel will have the ability to elect the board of directors of Kestrel Heat, including Messrs. Vermynen, Lawrence and Lubar. Messrs. Vermynen, Lawrence and Lubar are also members of the board of managers of Kestrel and, either directly or through affiliated entities, own equity interests in Kestrel. Kestrel owns all of the issued and outstanding membership interests of Kestrel Heat and M2. Kestrel Heat and M2 will receive an aggregate of 6,750,000 common units as a result of the recapitalization. M2 also will make a commitment to purchase all units which are not subscribed for in the rights offering of 19,687,500 common units. Kestrel Heat and M2, therefore, will receive an aggregate minimum of 6,750,000 common units and could receive an aggregate maximum of 26,437,500 common units as a result of the recapitalization. Mr. Vermynen also individually owns 50,000 common units and \$100,000 face amount of senior notes, which he owned prior to the commencement of the negotiations of the recapitalization transaction. See also Unit Ownership for additional information on the unit ownership by prospective directors and/or officers of Kestrel Heat who are currently officers and/or directors of Star Gas.



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Kestrel Heat intends to establish management incentive programs whereby executive officers will be offered an opportunity to invest in Kestrel Heat. Pursuant to the proposed second and amended restated partnership agreement that has been approved by unitholders and will be adopted as part of the recapitalization, Kestrel Heat, as the general partner of Star Gas Partners, is entitled to incentive distributions commencing fiscal 2009 if minimum quarterly distributions to common unitholders exceed certain target levels. Kestrel Heat also intends to compensate non-management directors for service on the board and respective board committees in customary amounts and types. The specific types and amounts of management incentive compensation arrangements and non-management director fees are expected to be formulated and finalized prior to consummation of the recapitalization.

## **Future Plans of Kestrel Heat**

Except as part of the recapitalization disclosed in this prospectus, Kestrel Heat does not have any specific intention with respect to Star Gas Partners that would involve any of the following transactions:

payment of extraordinary distributions;

issuance of additional equity to third parties;

refinancing, reducing or increasing existing indebtedness of Star Gas Partners;

additional purchases of interests in Star Gas Partners; and

mergers or other consolidation transactions involving Star Gas Partners.

However, if the recapitalization is consummated, Kestrel Heat will be able to consider those transactions and may recommend them to the unitholders of Star Gas Partners for approval or, if no other partnership approvals are required, effect those transactions as the general partner of Star Gas Partners. There is no assurance, however, as to when or whether any of the transactions referred to above might occur. Under applicable law, directors of Kestrel Heat as general partner of Star Gas Partners will owe certain fiduciary obligations to all of the unitholders of Star Gas Partners, not just M2 and affiliates of Kestrel. However, Kestrel's right to control the board of directors could have the effect of delaying, deterring or preventing tender offers or takeover attempts that some or a majority of Star Gas Partners' unitholders might consider in their best interests, including offers or attempts that might result in the payment of a premium over the market price for the units. If Star Gas Partners enters into a transaction, Kestrel Heat, M2 and Kestrel will participate in the benefits of that transaction to the extent of their ownership of interests in Star Gas Partners.

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**UNIT PURCHASE AGREEMENT**

*The following is a summary of the material provisions of the unit purchase agreement with Kestrel and its affiliates dated as of December 5, 2005, as amended on March 12, 2006 and March 30, 2006 (the "unit purchase agreement"). This summary does not include all of the provisions of the unit purchase agreement, the full text of which is incorporated into this prospectus by reference. Holders of common units should read the unit purchase agreement in its entirety.*

**Agreement to Sell and to Purchase Common Units**

The unit purchase agreement provides that subject to the terms and subject to the conditions set forth in the agreement, on the closing date Star Gas Partners shall sell to Kestrel Heat and M2, both wholly-owned subsidiaries of Kestrel:

- (a) 500,000 common units to Kestrel Heat;
- (b) 6,250,000 common units to M2;
- (c) 325,729 new general partner units to Kestrel Heat; and
- (d) a number of common units to M2 equal to the number of common units that are not subscribed for in the rights offering.

The purchase price for the common units referred to in (a) and (b) above is \$2.50 per unit and the purchase price for the common units referred to in (d) above is \$2.25 per unit. The general partner units will be issued for no additional consideration.

On April 5, 2006, the last trading day prior to the date of this prospectus, the closing sales price per common unit on the NYSE was \$2.61 per unit and the closing sales price per senior subordinated unit on the NYSE was \$2.16 per unit. On December 2, 2005, the last trading day prior to the public announcement of the recapitalization transaction with Kestrel, the c