

Cheniere Energy Partners, L.P.  
Form 10-Q  
November 07, 2008  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q**

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

For the quarterly period ended September 30, 2008

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File No. 001-33366

**Cheniere Energy Partners, L.P.**

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of incorporation or organization)

20-5913059

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

700 Milam Street, Suite 800

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**Houston, Texas**

**(Address of principal executive offices)**

**77002**

**(Zip Code)**

**(713) 375-5000**

**(Registrant's telephone number, including area code)**

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definition of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer

Non-accelerated filer  Smaller reporting company

(Do not check if a smaller reporting company)

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

The issuer had 26,416,357 common units and 135,383,831 subordinated units outstanding as of November 3, 2008.

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**CHENIERE ENERGY PARTNERS, L.P.**

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(in thousands, except unit data)

	September 30, 2008 (unaudited)	December 31, 2007
<b>ASSETS</b>		
<b>CURRENT ASSETS</b>		
Cash and cash equivalents	\$ 11	\$ 13
Restricted cash and cash equivalents	267,541	191,179
Accounts and interest receivable	3,029	5,584
Accounts receivable affiliate	6,118	
Advances to affiliate	4,250	1,709
Prepaid expenses and other	7,336	432
Total current assets	288,285	198,917
NON-CURRENT RESTRICTED CASH AND CASH EQUIVALENTS	151,752	453,843
NON-CURRENT RESTRICTED TREASURY SECURITIES	31,456	63,923
PROPERTY, PLANT AND EQUIPMENT, NET	1,482,959	1,127,289
DEBT ISSUANCE COSTS, NET	31,766	29,895
ADVANCES UNDER LONG-TERM CONTRACTS	12,763	28,497
ADVANCES TO AFFILIATE LNG HELD FOR COMMISSIONING	16,595	
OTHER	5,043	2,614
Total assets	\$ 2,020,619	\$ 1,904,978
<b>LIABILITIES AND PARTNERS DEFICIT</b>		
<b>CURRENT LIABILITIES</b>		
Accounts payable	\$ 3,531	\$ 63
Accounts payable affiliate	820	
Accrued liabilities	79,704	52,309
Accrued liabilities affiliate	8,764	1,048
Deferred revenue	1,500	
Deferred revenue affiliate	15,000	
Total current liabilities	109,319	53,420
LONG-TERM DEBT, NET OF DISCOUNT	2,177,161	2,032,000
LONG-TERM DEBT AFFILIATE	2,117	645
DEFERRED REVENUE	43,471	42,583
OTHER NON-CURRENT LIABILITIES	362	3,847
COMMITMENTS AND CONTINGENCIES		
<b>PARTNERS DEFICIT</b>		
Owners deficit, including deficit accumulated during development stage of \$171,329 at September 30, 2008 and \$121,404 at December 31, 2007		
Common unitholders (26,416,357 units issued and outstanding at September 30, 2008)	(7,746)	33,923

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Subordinated unitholders (135,383,831 units issued and outstanding at September 30, 2008)	(295,691)	(254,752)
General partner interest (2% interest with 3,302,045 units issued and outstanding at September 30, 2008)	(8,374)	(6,688)
<b>Total partners deficit</b>	<b>(311,811)</b>	<b>(227,517)</b>
Total liabilities and partners deficit	\$ 2,020,619	\$ 1,904,978

See accompanying notes to consolidated combined financial statements.

Index to Financial Statements**CHENIERE ENERGY PARTNERS, L.P.****A DEVELOPMENT STAGE ENTERPRISE****CONSOLIDATED COMBINED STATEMENTS OF OPERATIONS**

(in thousands, except per unit data)

(unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,		Period from October 20, 2003 (Date of Inception) to September 30, 2008
	2008	2007	2008	2007	2008
REVENUES	\$	\$	\$	\$	\$
EXPENSES					
Legal	16	52	104	128	2,487
Professional	792	272	1,590	475	4,032
Technical consulting					4,577
Land site rental	377	371	1,124	1,142	4,155
Depreciation expense	1,874	67	1,911	131	2,009
Insurance	340		381		381
Labor and overhead charge from affiliate	3,527	2,332	7,836	5,924	23,603
LNG receiving terminal repair and maintenance expense	2,751		2,751		2,751
Phase 2 Stage 1 development reimbursement to affiliate					4,527
Other	349	73	1,177	128	3,309
<b>TOTAL EXPENSES</b>	<b>10,026</b>	<b>3,167</b>	<b>16,874</b>	<b>7,928</b>	<b>51,831</b>
LOSS FROM OPERATIONS	(10,026)	(3,167)	(16,874)	(7,928)	(51,831)
OTHER INCOME (EXPENSE)					
Interest income	2,169	12,625	12,218	42,020	73,890
Interest expense, net	(17,737)	(20,570)	(47,630)	(70,053)	(151,754)
Loss on early extinguishment of debt					(23,761)
Derivative gain (loss), net	14,692		2,325		(17,909)
Other	5		36		36
<b>TOTAL OTHER EXPENSE</b>	<b>(871)</b>	<b>(7,945)</b>	<b>(33,051)</b>	<b>(28,033)</b>	<b>(119,498)</b>
<b>NET LOSS</b>	<b>\$ (10,897)</b>	<b>\$ (11,112)</b>	<b>\$ (49,925)</b>	<b>\$ (35,961)</b>	<b>\$ (171,329)</b>
Less:					
Net loss through March 25, 2007				(12,128)	
Net loss for partners from March 26, 2007 through September 30, 2007				\$ (23,833)	
Allocation of net loss:					
Limited partners' interest	(10,679)	(10,890)	(48,927)	(23,356)	
General partner's interest	(218)	(222)	(998)	(477)	

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Net loss for partners	\$ (10,897)	\$ (11,112)	\$ (49,925)	\$ (23,833)
Basic and diluted net loss per limited partner unit	\$ (0.07)	\$ (0.07)	\$ (0.31)	\$ (0.14)
Weighted average number of limited partner units outstanding from the beginning of the period through June 30, 2007 used for basic and diluted net loss per unit calculation:				
Common units	26,416	26,416	26,416	26,416
Subordinated units	135,384	135,384	135,384	135,384
	161,800	161,800	161,800	161,800

See accompanying notes to consolidated combined financial statements.

Index to Financial Statements**CHENIERE ENERGY PARTNERS, L.P.****A DEVELOPMENT STAGE ENTERPRISE****CONSOLIDATED COMBINED STATEMENTS OF PARTNERS DEFICIT**

(in thousands)

	<b>Partners /Owners Deficit</b>	<b>Common Units</b>	<b>Subordinated Units</b>	<b>General Partner Units</b>	<b>Total</b>
Balance at October 20, 2003	\$	\$	\$	\$	\$
Net loss	(2,763)				(2,763)
Balance at December 31, 2003	(2,763)				(2,763)
Distributions	(10,000)				(10,000)
Net loss	(4,654)				(4,654)
Balance at December 31, 2004	(17,417)				(17,417)
Capital contributions	161,562				161,562
Rescinded distribution	10,000				10,000
Change in fair value of derivative instrument	1,814				1,814
Net loss	(4,263)				(4,263)
Balance at December 31, 2005	151,696				151,696
Capital contributions	35,900				35,900
Distributions	(378,348)				(378,348)
Change in fair value of derivative instrument	(1,814)				(1,814)
Net loss	(60,772)				(60,772)
Balance at December 31, 2006	(253,338)				(253,338)
Net loss through March 25, 2007	(12,128)				(12,128)
Balance at March 25, 2007	(265,466)				(265,466)
Contribution of net deficit investment to unitholders	265,466	(35,434)	(224,556)	(5,476)	
Proceeds from initial public offering, net of issuance costs		98,442			98,442
Net loss from March 26, 2007 through December 31, 2007		(5,892)	(30,196)	(736)	(36,824)
Distributions		(23,193)		(476)	(23,669)
Balance at December 31, 2007		33,923	(254,752)	(6,688)	(227,517)
Net loss (unaudited)		(7,988)	(40,939)	(998)	(49,925)
Distributions (unaudited)		(33,681)		(688)	(34,369)
Balance at September 30, 2008 (unaudited)	\$	\$ (7,746)	\$ (295,691)	\$ (8,374)	\$ (311,811)

See accompanying notes to consolidated combined financial statements.



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(in thousands)

(unaudited)

	Nine Months Ended September 30,		Period from October 20, 2003 (Date of Inception) to September 30, 2008
	2008	2007	
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
Net loss	\$ (49,925)	\$ (35,961)	\$ (171,329)
Adjustments to reconcile net loss to net cash used in operating activities:			
Depreciation	1,911	131	2,009
Non-cash derivative loss	(3,751)		(4,090)
Interest income on restricted cash and cash equivalents	(14,332)	(42,020)	(63,970)
Use of restricted cash and cash equivalents	21,018	66,328	124,061
Amortization of debt issuance costs	3,086	2,843	7,574
Loss on early extinguishment of debt			23,750
Changes in operating assets and liabilities:			
Accounts payable and accrued liabilities	26,236	8,550	28,266
Accounts payable and accrued liabilities affiliate	8,536	(156)	9,596
Accounts and interest receivable	2,555		(2,671)
Accounts receivable affiliate	(6,118)		(6,118)
Deferred revenue	17,388		59,971
Advances to affiliate	(2,544)		(2,544)
Prepaid and other	(5,534)	7	(4,920)
<b>NET CASH USED IN OPERATING ACTIVITIES</b>	<b>(1,474)</b>	<b>(278)</b>	<b>(415)</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Use of (investment in) restricted cash and cash equivalents	357,520	331,402	(341,380)
LNG receiving terminal construction-in-process, net	(333,848)	(307,066)	(1,389,137)
Advances to affiliate LNG held for commissioning, net of amounts transferred to			
LNG terminal construction-in-process	(16,595)		(16,595)
Advances under long-term contracts	(7,077)	(34,567)	(52,713)
Investment in restricted treasury securities		(75,023)	(63,923)
Other		(977)	(1,996)
<b>NET CASH USED IN INVESTING ACTIVITIES</b>		<b>(86,231)</b>	<b>(1,865,744)</b>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>			
Use of (investment in) restricted cash and cash equivalents	(106,012)	740	(105,287)
Borrowings from long-term note affiliate	1,472	282	2,117
Proceeds from issuance of common units		98,442	98,442
Debt issuance costs	(4,586)	(740)	(66,371)
Proceeds from issuance of Sabine Pass LNG notes	144,965		2,176,965
Proceeds from subordinated note affiliate			37,377
Repayment of subordinated note affiliate			(37,377)
Borrowings from Sabine Pass credit facility			383,400
Repayment of Sabine Pass credit facility			(383,400)

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Distribution to owners	(34,368)	(12,213)	(436,385)
Affiliate payable	1		35,117
Capital contributions by partner			161,572
NET CASH PROVIDED BY FINANCING ACTIVITIES	1,472	86,511	1,866,170
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(2)	2	11
CASH AND CASH EQUIVALENTS beginning of period	13	7	
CASH AND CASH EQUIVALENTS end of period	\$ 11	\$ 9	\$ 11

See accompanying notes to consolidated combined financial statements.

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**CHENIERE ENERGY PARTNERS, L.P.**

**A DEVELOPMENT STAGE ENTERPRISE**

**NOTES TO CONSOLIDATED COMBINED FINANCIAL STATEMENTS**

**(unaudited)**

**NOTE 1 Nature of Operations**

Cheniere Energy Partners, L.P. (Cheniere Partners) is a publicly-held limited partnership. As of September 30, 2008, Cheniere Energy, Inc. (Cheniere) owned 90.6% of the partnership through its wholly-owned subsidiaries, Cheniere Subsidiary Holdings, LLC (Subsidiary Holdings), Cheniere Common Units Holding, LLC and Cheniere Energy Partners GP, LLC (the General Partner). Cheniere Partners is a Delaware limited partnership formed on November 21, 2006 to own and operate the Sabine Pass liquefied natural gas (LNG) receiving and regasification facility in western Cameron Parish, Louisiana on the Sabine Pass Channel (the Sabine Pass LNG receiving terminal). Cheniere Partners and Cheniere LNG Holdings, LLC (Holdings), as a selling unitholder, completed an initial public offering (the Cheniere Partners Offering) of Cheniere Partners common units on March 26, 2007.

The following entities were included on a combined basis in the accompanying Consolidated Combined Financial Statements for periods prior to the Cheniere Partners Offering because they were entities under common control:

Cheniere Partners;

Cheniere Energy Investments, LLC (Cheniere Investments) is a Delaware limited liability company owned by Cheniere Partners and was formed on November 21, 2006 to hold 100% of the ownership interests in Sabine Pass GP and Sabine Pass LP;

Sabine Pass LNG-GP, Inc. (Sabine Pass GP) is a Delaware corporation that was owned by Holdings and was formed in 2004 to be the general partner of Sabine Pass LNG, L.P. (Sabine Pass LNG);

Sabine Pass LNG-LP, LLC (Sabine Pass LP) is a Delaware limited liability company that was owned by Holdings and was formed in 2004 to be the limited partner of Sabine Pass LNG; and

Sabine Pass LNG is a Delaware limited partnership formed with one general partner, Sabine Pass GP, and one limited partner, Sabine Pass LP, which owns the entire interest in the Sabine Pass LNG receiving terminal. Sabine Pass LNG is in the development stage, and the purpose of this limited partnership is to own and operate the Sabine Pass LNG receiving terminal.

At the closing of the Cheniere Partners Offering on March 26, 2007, the equity interests in Sabine Pass GP and Sabine Pass LP were contributed to Cheniere Investments, thereby resulting in Sabine Pass GP, Sabine Pass LP and Sabine Pass LNG becoming indirect, wholly-owned subsidiaries of Cheniere Partners. From and after the closing of the Cheniere Partners Offering, Cheniere Investments and these subsidiaries are consolidated with Cheniere Partners in the accompanying financial statements. As used in these Notes to Consolidated Combined Financial Statements, the terms Cheniere Partners, we, us and our refer to Cheniere Partners and its consolidated subsidiaries effective with the closing of the Cheniere Partners Offering and the foregoing entities on a combined basis (the Combined Predecessor Entities) prior to the closing of the Cheniere Partners Offering, unless otherwise stated or indicated by context.

With the exception of Sabine Pass GP, we are not subject to either federal or state income tax, as the partners are taxed individually on their proportionate share of our earnings. Sabine Pass GP is a corporation and is subject to both federal and state income tax. However, since Sabine Pass GP's inception, its activities have been strictly limited to holding a non-income or loss bearing general partner interest in Sabine Pass LNG and, thus, this entity has not realized any taxable net income to date and is not expected to realize any taxable net income in the future.



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**A DEVELOPMENT STAGE ENTERPRISE**

**NOTES TO CONSOLIDATED COMBINED FINANCIAL STATEMENTS (Continued)**

**(unaudited)**

The accompanying unaudited Consolidated Combined Financial Statements of Cheniere Partners have been prepared in accordance with generally accepted accounting principles in the United States ( GAAP ) for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In our opinion, all adjustments, consisting only of normal recurring adjustments necessary for a fair presentation, have been included. All significant intercompany transactions and balances have been eliminated. Results of operations for the three and nine months ended September 30, 2008 are not necessarily indicative of results for the year ending December 31, 2008.

For further information, refer to the financial statements and footnotes included in our annual report on Form 10-K for the year ended December 31, 2007.

**NOTE 2 Development Stage Operations**

We were formed on October 20, 2003 (the earliest formation date of the Combined Predecessor Entities). Operations to date have been devoted to pre-construction and construction activities and minimal operating activities. Our ultimate profitability will depend on, among other factors, the successful completion of construction of the Sabine Pass LNG receiving terminal and commencement of commercial operation. As of September 30, 2008, we had a cumulative net loss of \$171.3 million since inception.

**NOTE 3 Advances to Affiliate-LNG Held for Commissioning**

In connection with the construction of the Sabine Pass LNG receiving terminal, we require LNG to perform certain commissioning activities, as follows:

**Cool down** A minimum amount of LNG will be used to cool down the LNG receiving terminal. Cool down represents the amount of LNG required to cool the LNG receiving terminal to its normal operating temperature.

**LNG heel** A certain amount of LNG will be used to establish a level of LNG inventory in each LNG storage tank and in the LNG receiving terminal piping in order for the LNG receiving terminal to function properly.

**Equipment commissioning** The remaining amount of the LNG will be used to commission the equipment in the LNG receiving terminal to ensure that it performs at designed specifications. Equipment commissioning will result in natural gas being sold. LNG purchased on Sabine Pass LNG's behalf by Cheniere Marketing, LLC ( Cheniere Marketing ), formerly Cheniere Marketing, Inc., has been funded by Sabine Pass LNG and is recorded at historical cost and classified as a non-current asset on our Consolidated Balance Sheets as Advances to Affiliate LNG Held for Commissioning (see Note 11 Related Party Transactions); for this LNG, Cheniere Marketing holds title to the LNG at all times, sells all regassified LNG and remits the net proceeds from such sales back to Sabine Pass LNG. The LNG used in the commissioning process is capitalized net of amounts received from the sale of natural gas.

As of September 30, 2008, Sabine Pass LNG or Cheniere Marketing on its behalf had acquired a total of three LNG commissioning cargoes for the Sabine Pass LNG receiving terminal, and we have unloaded the LNG into the Sabine Pass LNG receiving terminal. As of September 30, 2008, our Advances to Affiliate LNG Held for Commissioning were \$16.6 million.



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**A DEVELOPMENT STAGE ENTERPRISE**

**NOTES TO CONSOLIDATED COMBINED FINANCIAL STATEMENTS (Continued)**

**(unaudited)**

**NOTE 4 Restricted Cash and Cash Equivalents and U.S. Treasury Securities**

Restricted cash and cash equivalents and U.S. treasury securities are comprised of cash that has been contractually restricted as to usage or withdrawal, as follows:

**Sabine Pass LNG Receiving Terminal Construction Reserve**

In November 2006, Sabine Pass LNG issued an aggregate principal amount of \$2,032.0 million of Senior Secured Notes consisting of \$550.0 million of 7<sup>1</sup>/<sub>4</sub>% Senior Secured Notes due 2013 (the 2013 Notes ) and \$1,482.0 million of 7% Senior Secured Notes due 2016 (the 2016 Notes and collectively with the 2013 Notes, the Sabine Pass LNG notes ) (see Note 8 Long-Term Debt ). In September 2008, Sabine Pass LNG issued an additional \$183.5 million, before discount, of the 2016 Notes whose terms were identical to the previously outstanding 2016 Notes. The additional issuance and the previously outstanding 2016 Notes are treated as a single series of notes under the indenture (see Note 8 Long-Term Debt ). Under the terms and conditions of the Sabine Pass LNG notes, we were required to fund a cash reserve account for approximately \$987 million to pay construction costs for the Sabine Pass LNG receiving terminal. The cash account is controlled by a collateral trustee, and therefore, is shown as restricted cash and cash equivalents on our Consolidated Balance Sheets. As of September 30, 2008 and December 31, 2007, \$48.2 million and \$40.2 million related to accrued construction costs were classified as part of current restricted cash and cash equivalents, and \$57.4 million and \$380.2 million related to remaining construction costs were classified as a non-current asset on our Consolidated Balance Sheets, respectively.

**Sabine Pass LNG Notes Debt Service Reserve**

As described above, Sabine Pass LNG consummated a private offering of an aggregate principal amount of \$2,215.5 million of Sabine Pass LNG notes (see Note 8 Long-Term Debt ). Under the terms and conditions of the Sabine Pass LNG notes, Sabine Pass LNG was required to fund a cash reserve account for \$335.0 million related to future interest payments on the Sabine Pass LNG notes. Beginning in July 2008, the indenture governing the Sabine Pass LNG notes requires that one semi-annual interest payment be maintained in a reserve account. As of September 30, 2008 and December 31, 2007, \$82.4 million and \$61.8 million, respectively, had been classified as part of non-current restricted cash and cash equivalents related to the semi-annual interest payment maintained in this reserve account. In addition, on a monthly basis, one-sixth of the semi-annual interest payment must be deposited into another reserve account. As of September 30, 2008 and December 31, 2007, \$54.9 million and \$151.0 million, respectively, related to the payment of interest due within twelve months was maintained in this separate reserve account and had been classified as part of current restricted cash and cash equivalents. These cash accounts are controlled by a collateral trustee, and therefore, are shown as restricted cash and cash equivalents on our Consolidated Balance Sheets.

**Distribution Reserve**

At the closing of our initial public offering, we funded a distribution reserve of \$98.4 million, which was invested in U.S. treasury securities. The distribution reserve, including interest earned thereon, will be used to pay quarterly distributions of \$0.425 per common unit for all common units, as well as related distributions to our general partner, through the distribution made in respect of the quarter ending June 30, 2009. The U.S. treasury securities were acquired at a discount from their maturity values equal to an average of approximately 4.87% per year. As of September 30, 2008 and December 31, 2007, we classified the \$31.5 million and \$63.9 million balance of U.S. treasury securities as non-current restricted U.S. treasury securities on our Consolidated

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Balance Sheets, respectively, as these securities had original maturities greater than three months. In addition, as of September 30, 2008 and December 31, 2007, \$11.9 million and \$11.8 million, respectively, related to our distribution reserve was classified as non-current restricted cash on our Consolidated Balance Sheets.

**Other Restricted Cash and Cash Equivalents**

As of September 30, 2008, \$164.4 million had been classified as part of current restricted cash and cash equivalents on our Consolidated Balance Sheet. This restricted cash and cash equivalents is related to cash and cash equivalents controlled by Sabine Pass LNG and not available to us for use under certain covenants in the indenture governing the Sabine Pass LNG notes.

**NOTE 5 Property, Plant and Equipment**

Property, plant and equipment consists of LNG receiving terminal construction-in-process expenditures, LNG site and related costs and fixed assets, as follows (in thousands):

	September 30, 2008	December 31, 2007
<b>LNG TERMINAL COSTS</b>		
LNG receiving terminal	\$ 912,455	\$
LNG receiving terminal construction-in-process	571,096	1,126,162
LNG site and related costs, net	186	191
Accumulated depreciation	(1,794)	
Total LNG receiving terminal costs, net	\$ 1,481,943	\$ 1,126,353
<b>FIXED ASSETS</b>		
Computers and office equipment	\$ 200	\$ 203
Vehicles	422	522
Machinery and equipment	751	411
Other	243	68
Accumulated depreciation	(600)	(268)
Total fixed assets, net	\$ 1,016	\$ 936
PROPERTY, PLANT AND EQUIPMENT, net	\$ 1,482,959	\$ 1,127,289

Costs associated with the construction of the Sabine Pass LNG receiving terminal have been capitalized as construction-in-process since the date the project satisfied our criteria for capitalization. For the nine months ended September 30, 2008 and 2007, and from date of inception through September 30, 2008, we capitalized \$69.4 million, \$46.1 million and \$163.2 million of interest expense related to the construction of the Sabine Pass LNG receiving terminal, respectively.



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We began depreciating equipment and facilities associated with the initial 2.6 Bcf/d of sendout capacity and 10.1 Bcf of storage capacity of the Sabine Pass LNG receiving terminal when they were ready for use in the third quarter of 2008. The Sabine Pass LNG receiving terminal is depreciated using the straight-line depreciation method applied to groups of LNG receiving terminal assets with varying useful lives. The identifiable components of the Sabine Pass LNG receiving terminal with similar estimated useful lives have a depreciable range between 10 and 50 years.

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We have entered into certain engineering, procurement and construction contracts and purchase agreements related to the construction of the Sabine Pass LNG receiving terminal that require us to make payments to fund costs that will be incurred or equipment that will be received in the future. Advances made under long-term contracts on purchase commitments are carried at face value and transferred to property, plant and equipment as the costs are incurred or equipment is received. As of September 30, 2008 and December 31, 2007, our Advances Under Long-Term Contracts were \$12.8 million and \$28.5 million, respectively.

**NOTE 7 Accrued Liabilities**

As of September 30, 2008 and December 31, 2007, accrued liabilities consisted of the following (in thousands):

	September 30, 2008	December 31, 2007
Interest and related debt fees	\$ 55,349	\$ 13,005
LNG terminal construction costs	21,477	39,051
Affiliate	8,764	1,048
Hurricane Ike repair and maintenance costs	2,751	
Other	127	253
Accrued liabilities	\$ 88,468	\$ 53,357

**NOTE 8 Long-Term Debt**

As of September 30, 2008 and December 31, 2007, our long-term debt consisted of the following (in thousands):

	September 30, 2008	December 31, 2007
Sabine Pass LNG notes, net of discount	\$ 2,177,161	\$ 2,032,000
Long-Term note to affiliate	2,117	645
Total Long-Term Debt	\$ 2,179,278	\$ 2,032,645

**Sabine Pass LNG Notes**

In November 2006, Sabine Pass LNG issued an aggregate principal amount of \$2,032.0 million of Sabine Pass LNG notes, consisting of \$550.0 million of the 2013 Notes and \$1,482.0 million of the 2016 Notes. In September 2008, Sabine Pass LNG issued an additional \$183.5 million of 2016 Notes whose terms were identical to the previously outstanding 2016 Notes. The net proceeds received from the additional issuance of 2016 Notes were \$145.0 million. The additional issuance and the previously outstanding 2016 Notes are treated as a single series of notes under the indenture. We placed \$100.0 million of the \$145.0 million net proceeds from the additional issuance of the 2016 Notes into a construction account to pay construction expenses of cost overruns related to the construction, cool down, commissioning and completion of the Sabine Pass

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LNG receiving terminal. In addition, we placed \$40.8 million of the remaining net proceeds into an account in accordance with the cash waterfall requirements of the security deposit agreement, which are used by Sabine Pass LNG for working capital and other general business purposes.

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**CHENIERE ENERGY PARTNERS, L.P.**

**A DEVELOPMENT STAGE ENTERPRISE**

**NOTES TO CONSOLIDATED COMBINED FINANCIAL STATEMENTS (Continued)**

**(unaudited)**

We placed \$335.0 million of the net proceeds from the original issuance of the Sabine Pass LNG notes in a reserve account to fund scheduled interest payments on the original Sabine Pass LNG notes. Interest on the Sabine Pass LNG notes is payable semi-annually in arrears on May 30 and November 30 of each year. The Sabine Pass LNG notes are secured on a first-priority basis by a security interest in all of Sabine Pass LNG's equity interests and substantially all of its operating assets.

Under the indenture governing the Sabine Pass LNG notes, except for permitted tax distributions, Sabine Pass LNG may not make distributions until certain conditions are satisfied. The indenture requires that Sabine Pass LNG apply its net operating cash flow (i) first, to fund with monthly deposits its next semiannual payment of approximately \$82.4 million of interest on the Sabine Pass LNG notes, and (ii) second, to fund a one-time, permanent debt service reserve fund equal to one semiannual interest payment of approximately \$82.4 million on the Sabine Pass LNG notes. Distributions from Sabine Pass LNG will be permitted only after satisfying the foregoing funding requirements, after satisfying a fixed charge coverage ratio test of 2:1 and after satisfying other conditions specified in the indenture.

**Long-Term Note Affiliate**

In March 2007, we entered into a \$12.0 million unsecured revolving credit note with Cheniere Energy Shared Services, Inc., formerly Cheniere LNG Financial Services, Inc., a wholly-owned subsidiary of Cheniere, to be paid upon demand but no sooner than January 1, 2010, or the date on which we have sufficient available cash. The purpose of this note is to provide funds for the payment of certain public company and other expenses that cannot be funded by the Sabine Pass LNG notes. Borrowings under this note bear interest at a fixed 7.50% rate with unpaid interest compounded semi-annually. As of September 30, 2008 and December 31, 2007, the outstanding principal plus interest was \$2.1 million and \$0.6 million, respectively.

**NOTE 9 Description of Equity Interests**

The common units and subordinated units represent limited partner interests in us. The holders of the units are entitled to participate in partnership distributions and exercise the rights and privileges available to limited partners under our partnership agreement. In May 2007, Holdings contributed all of its 135,383,831 subordinated units that it received in connection with the initial public offering to Subsidiary Holdings, and in April 2008, Holdings contributed all of its 10,891,357 common units that it received in connection with the initial public offering to Cheniere Common Units Holding, LLC.

The common units and general partner units have the right to receive minimum quarterly distributions of \$0.425 and \$0.069 per unit, respectively, plus any arrearages thereon, before any distribution is made to the holders of the subordinated units.

During the subordination period, the subordinated units will not be entitled to receive any distributions until the common units have received \$0.425 per unit plus any arrearages from prior quarters. Subordinated units will convert into common units on a one-for-one basis when the subordination period ends. The subordination period will end when we meet financial tests specified in the partnership agreement.

The general partner interest is entitled to at least 2% of all distributions made by us. In addition, the general partner holds incentive distribution rights, which allow the general partner to receive a higher percentage of quarterly distributions of available cash from operating surplus after the minimum distributions have been achieved and as additional target levels are met. The higher percentages range from 15% up to 50%.

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(unaudited)

**NOTE 10 Financial Instruments**

On behalf of Sabine Pass LNG, Cheniere Marketing has entered into financial derivatives to hedge the exposure to variability in expected future cash flows attributable to the future sale of natural gas from our LNG commissioning cargoes ( LNG commissioning cargo derivatives ). The net cost (LNG commissioning cargo purchase price less natural gas sales proceeds) of our LNG commissioning cargoes is capitalized on our Consolidated Balance Sheets as it is directly related to the LNG receiving terminal construction and is incurred to place the LNG receiving terminal in usable condition. However, changes in the fair value of our LNG commissioning cargo derivatives are reported in earnings because they are not able to be designated as a qualifying hedge in accordance with FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities*.

Effective January 1, 2008, we adopted Statement of Financial Accounting Standards ( SFAS ) No. 157, *Fair Value Measurements* ( SFAS 157 ) and SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities-Including an amendment of FASB Statement No. 115* ( SFAS 159 ). As a result of the adoption, we elected not to measure any additional financial assets or liabilities at fair value, other than those which were recorded at fair value prior to the adoption.

The estimated fair value of financial instruments is the amount at which the instrument could be exchanged currently between willing parties. The financial assets at September 30, 2008 measured at fair value on a recurring basis are summarized below (in thousands):

	Quoted Prices in Active Markets for Identical Instruments (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Carrying Value at September 30, 2008
Derivatives receivables	\$ 3,750	\$	\$	\$ 3,750
Total assets at fair value	\$ 3,750	\$	\$	\$ 3,750

Derivatives receivables reflect LNG commissioning cargo derivative positions held by Cheniere Marketing on behalf of Sabine Pass LNG related to natural gas swaps entered into to mitigate the price risk from sales of excess LNG purchased for commissioning and performance testing.

SFAS No. 107, *Disclosures About Fair Value of Financial Instruments* ( SFAS 107 ) requires the disclosure of the estimated fair value of financial instruments, including those financial instruments for which the SFAS 159 fair value option was not elected. The carrying amounts reported on the Consolidated Balance Sheets for cash and cash equivalents, restricted cash and cash equivalents, accounts receivables, interest receivables, and accounts payables approximate fair value due to their short-term nature. The carrying amounts and fair values of financial instruments for which SFAS 159 was not elected are as follows:

Financial Instruments (in thousands):

September 30, 2008		December 31, 2007	
Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value

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2013 Notes (1)	\$ 550,000	\$ 448,250	\$ 550,000	\$ 525,250
2016 Notes, net of discount (1)	1,627,161	1,293,593	1,482,000	1,404,195
Note to Affiliate (2)	2,117	2,117	645	645
Restricted U.S. treasury securities (3)	31,456	34,107	63,923	66,984

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**(unaudited)**

- (1) The fair value of the Sabine Pass LNG notes, net of discount, was based on quotations obtained from broker-dealers who made markets in these and similar instruments as of September 30, 2008 and December 31, 2007, as applicable.
- (2) The Note to Affiliate bears interest at a fixed 7.50% rate. Management estimates that the carrying amount is a reasonable approximation of the fair value as of September 30, 2008 and December 31, 2007, as applicable.
- (3) The fair value of our Restricted U.S. treasury securities was based on quotations obtained from broker-dealers who made markets in these and similar instruments as of September 30, 2008 and December 31, 2007, as applicable.

**NOTE 11 Related Party Transactions**

As of September 30, 2008 and December 31, 2007, we had \$4.3 million and \$1.7 million, respectively, of Advances to Affiliates. As of September 30, 2008, we had \$16.6 million of Advances to Affiliate LNG Held for Commissioning on our Consolidated Balance Sheets.

Under the LNG lease agreement described below, we had \$16.6 million recorded as Advance to Affiliates LNG Held for Commissioning on our Consolidated Balance Sheets related to the purchase by Cheniere Marketing of commissioning cargoes as of September 30, 2008.

Under the service agreements described below, we paid \$1.3 million during each of the three-month periods ended September 30, 2008 and 2007. For each of the nine-month periods ended September 30, 2008 and 2007, we paid \$3.9 million. For the period from October 20, 2003 (date of inception) to September 30, 2008, we paid \$18.3 million.

**LNG Lease Agreement**

In September 2008, Sabine Pass LNG entered into an agreement in the form of a lease with Cheniere Marketing that enabled Sabine Pass LNG to hedge the exposure to variability in expected future cash flows of Sabine Pass LNG's commissioning cargoes. The agreement permits Cheniere Marketing to deliver LNG to the Sabine Pass LNG receiving terminal and to receive regasified LNG for redelivery as natural gas in exchange for the use of the properties of the LNG to cool down the Sabine Pass LNG receiving terminal. Under the terms of the agreement, Sabine Pass LNG pays Cheniere Marketing a fixed fee based on the delivered quantity of LNG in each LNG cargo. Sabine Pass LNG assumes full price risk of the purchase and sale of the LNG and also finances all activities relating to the LNG. Cheniere Marketing holds title to the LNG at all times and sells all redelivered LNG and remits the net proceeds from such sales back to Sabine Pass LNG.

LNG purchased on Sabine Pass LNG's behalf by Cheniere Marketing that has been funded by Sabine Pass LNG is recorded at historical cost and classified as a non-current asset on our Consolidated Balance Sheets as Advances to Affiliate LNG Held for Commissioning. LNG that is lost, used as fuel or sold results in the reduction of Advances to Affiliate LNG Held for Commissioning on our Consolidated Balance Sheets at historical cost. During the second quarter of 2008, Sabine Pass LNG advanced Cheniere Marketing funds to purchase LNG. At September 30, 2008, we had \$16.6 million recorded as Advances to Affiliate LNG Held for Commissioning on our Consolidated Balance Sheets related to the purchase of commissioning cargoes. In addition, during the second quarter of 2008, Sabine Pass LNG incurred fixed fees from Cheniere Marketing of \$0.6 million that we capitalized as Property, Plant and Equipment on our Consolidated Balance Sheets.

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**NOTES TO CONSOLIDATED COMBINED FINANCIAL STATEMENTS (Continued)**

**(unaudited)**

**Services Agreements**

In February 2005, Sabine Pass LNG entered into a 20-year operation and maintenance agreement with a wholly-owned subsidiary of Cheniere Energy pursuant to which we receive all necessary services required to construct, operate and maintain the Sabine Pass LNG receiving terminal. Prior to substantial completion of the Sabine Pass LNG receiving terminal, Sabine Pass LNG is required to pay a fixed monthly fee of \$95,000 (indexed for inflation beginning in 2010) under the agreement. The fixed monthly fee will increase to \$130,000 (indexed for inflation beginning in 2010) upon substantial completion of Sabine Pass LNG's EPC contract with Bechtel, and the counterparty will thereafter be entitled to a bonus equal to 50% of the salary component of labor costs in certain circumstances to be agreed upon between Sabine Pass LNG and the counterparty at the beginning of each operating year. In addition, Sabine Pass LNG is required to reimburse the counterparty for its operating expenses, which are comprised primarily of labor expenses.

In February 2005, Sabine Pass LNG entered into a 20-year management services agreement with its general partner, which is a wholly-owned subsidiary of us, pursuant to which its general partner was appointed to manage the construction and operation of the Sabine Pass LNG receiving terminal, excluding those matters provided for under the operation and maintenance agreement described in the paragraph above. In August 2008, the general partner of Sabine Pass LNG assigned all of its rights and obligations under the management services agreement to Cheniere LNG Terminals, Inc. (Cheniere Terminals), a wholly-owned subsidiary of Cheniere Energy. Prior to substantial completion of the Sabine Pass LNG receiving terminal, Sabine Pass LNG is required to pay Cheniere Terminals a monthly fixed fee of \$340,000 (indexed for inflation beginning in 2010); thereafter, the monthly fixed fee will increase to \$520,000 (indexed for inflation beginning in 2010).

We entered into a services agreement with Cheniere Terminals pursuant to which we will pay Cheniere Terminals an annual administrative fee of \$10 million (adjusted for inflation after January 1, 2007) commencing January 1, 2009 for the provision of various general and administrative services for our benefit following the closing of our initial public offering. In addition, we will reimburse Cheniere Terminals for its services in an amount equal to the sum of all out-of-pocket costs and expenses incurred by Cheniere Terminals that are directly related to our business or activities.

During the three and nine months ended September 30, 2008, we paid an aggregate of \$1.3 million and \$3.9 million, respectively, under the foregoing services agreement from restricted cash and cash equivalents. For the period from October 20, 2003 (date of inception) to September 30, 2008, we paid \$18.3 million. Until substantial completion of the Sabine Pass LNG receiving terminal and revenues are received under the TUAs, we anticipate continuing to utilize restricted cash and cash equivalents to satisfy our obligations under these service agreements.

**Agreement to Fund Sabine Pass LNG's Cooperative Endeavor Agreements**

In July 2007, Sabine Pass LNG executed Cooperative Endeavor Agreements (CEAs) with various Cameron Parish, Louisiana taxing authorities that allow them to accelerate certain of Sabine Pass LNG's property tax payments scheduled to begin in 2019. This ten-year initiative represents an aggregate \$25.0 million commitment, and will make resources available to the Cameron Parish taxing authorities on an accelerated basis in order to aid in their reconstruction efforts following Hurricane Rita. In exchange for Sabine Pass LNG's advance payments of ad valorem taxes, Cameron Parish will grant Sabine Pass LNG a dollar for dollar credit against future ad valorem taxes to be levied against the Sabine Pass LNG receiving terminal starting in 2019. In September 2007, Sabine Pass LNG entered into an agreement with Cheniere Marketing pursuant to which Cheniere Marketing will advance Sabine Pass LNG any and all amounts payable under the CEAs in exchange for



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**(unaudited)**

a similar amount of credits against future ad valorem reimbursements it would owe Sabine Pass LNG under its TUA starting in 2019. These advance ad valorem tax payments were recorded to Other Assets on our Consolidated Balance Sheets, and payments from Cheniere Marketing that we utilized to make the early payment of taxes were recorded as Deferred Revenue on the Consolidated Balance Sheets. As of September 30, 2008 and December 31, 2007, we had \$5.0 million and \$2.6 million of Other Assets and Deferred Revenue, respectively, resulting from accelerated ad valorem tax payments.

**Contracts for Sale and Purchase of Natural Gas**

In 2007, Sabine Pass LNG entered into the following natural gas purchase and sale contracts with Cheniere Marketing:

*Contract for the Sale of Natural Gas from Commissioning Cargoes*

We require several LNG cargoes to cool down and commission the Sabine Pass LNG receiving terminal at the end of the construction process. Sabine Pass LNG entered into a contract with Cheniere Marketing for the sale of natural gas regasified from commissioning LNG cargoes at a sales price equal to the actual market price received by Cheniere Marketing in reselling the natural gas less any third-party costs incurred by Cheniere Marketing in respect of the receipt, delivery and resale of the natural gas, and less an administrative fee paid to Cheniere Marketing. Sabine Pass LNG sold zero and \$16.9 million of natural gas to Cheniere Marketing under this contract during the three and nine months ended September 30, 2008, respectively. For the period from October 20, 2003 (date of inception) to September 30, 2008, Sabine Pass LNG sold \$16.9 million of natural gas to Cheniere Marketing under this contract.

*Sale of Natural Gas from Boil-off*

Sabine Pass LNG entered into a contract for the sale to Cheniere Marketing of natural gas that has boiled off from LNG inventory in the Sabine Pass LNG receiving terminal at a sales price equal to the actual market price received by Cheniere Marketing in reselling the natural gas less any third-party costs incurred by Cheniere Marketing in respect of the receipt, delivery and resale of the natural gas and less an administrative fee paid to Cheniere Marketing. Sabine Pass LNG did not sell any natural gas to Cheniere Marketing under this contract for the period from October 20, 2003 (date of inception) to September 30, 2008.

*Purchase of Natural Gas for Fuel*

Sabine Pass LNG entered into a contract for the purchase of natural gas from Cheniere Marketing to use as fuel at the Sabine Pass LNG receiving terminal at a sales price equal to the actual purchase cost paid by Cheniere Marketing to suppliers of the natural gas less any third-party costs incurred by Cheniere Marketing in respect of the receipt, purchase, and delivery of the natural gas to the Sabine Pass LNG receiving terminal and less an administrative fee paid to Cheniere Marketing. During the three and nine months ended September 30, 2008, Sabine Pass LNG paid zero and \$2.9 million to Cheniere Marketing under this contract. For the period from October 20, 2003 (date of inception) to September 30, 2008, Sabine Pass LNG paid \$3.6 million to Cheniere Marketing under this contract.

**Contract for the Purchase of LNG Commissioning Cargoes**

In November 2007, Sabine Pass LNG entered into a contract with Cheniere Marketing to procure and deliver to the Sabine Pass LNG receiving terminal the LNG cargoes it requires for commissioning. Sabine Pass

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**(unaudited)**

LNG will reimburse Cheniere Marketing for its actual third-party costs incurred in obtaining these cargoes. During the three and nine months ended September 30, 2008, Sabine Pass LNG paid zero and \$25.6 million to Cheniere Marketing under this contract for its initial LNG commissioning cargo, respectively. For the period from October 20, 2003 (date of inception) to September 30, 2008, we paid \$25.6 million to Cheniere Marketing under this contract for the purchase of LNG commissioning cargoes.

**Contract for the Sale of Retained LNG**

As partial compensation for the terminaling services that Sabine Pass LNG provides its customers at the Sabine Pass LNG receiving terminal, Sabine Pass LNG retains 2% of the LNG that customers bring to the Sabine Pass LNG receiving terminal, which Sabine Pass LNG will use primarily as fuel for revaporization and self-generated power. In September 2007, Sabine Pass LNG entered into a contract with Cheniere Marketing for the sale of excess retainage at a market index-related sales price. Sabine Pass LNG did not sell any excess retainage to Cheniere Marketing under this contract for the period from October 20, 2003 (date of inception) to September 30, 2008.

**Contract for the Exclusive Use of a LNG Vessel During the Commissioning Process**

J & S Cheniere S.A. ( J&S Cheniere ), an indirect wholly-owned subsidiary of Cheniere, and Cheniere Marketing were parties to a time charter agreement for the Celestine River LNG vessel. In March 2008, Sabine Pass LNG entered into a contract with J&S Cheniere and Cheniere Marketing for exclusive use of this LNG vessel during our commissioning process until the Sabine Pass LNG receiving terminal's commercial start date. Sabine Pass LNG is responsible for all amounts that would otherwise be payable by J&S Cheniere or Cheniere Marketing under their time charter agreement. For the three and nine months ended September 30, 2008, we capitalized zero and \$16.3 million, respectively, related to LNG vessel costs under this contract.

**Contract for the Exclusive Use of Tugs During the Commissioning Process**

Sabine Pass Tug Services, LLC ( Sabine Pass Tug Services ), an indirect wholly-owned subsidiary of Cheniere, and Cheniere Marketing are parties to a marine services sharing agreement for the use of tug boats ( tugs ). In March 2008, Sabine Pass LNG entered into a contract with Sabine Pass Tug Services and Cheniere Marketing for exclusive use of the tugs during our commissioning process until the Sabine Pass LNG receiving terminal's commercial start date. Sabine Pass LNG is responsible for all amounts that would otherwise be payable by Sabine Pass Tug Services and Cheniere Marketing under their marine services sharing agreement. For the three and nine months ended September 30, 2008, we capitalized \$1.8 million and \$4.9 million, respectively, related to tug costs under this contract.

**TUA Agreement**

Cheniere Marketing has reserved approximately 2.0 Bcf/d of regasification capacity under a firm commitment TUA and has prepaid to Sabine Pass LNG capacity payments of \$5.0 million per month for the last three months of 2008 and has agreed to make monthly payments to Sabine Pass LNG aggregating approximately \$250 million per year through at least the third quarter of 2028. Cheniere has guaranteed Cheniere Marketing's obligations under its TUA.

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The following table provides supplemental disclosure of cash flow information (in thousands):

	Nine Months Ended September 30,		Period from October 20, 2003 (Date of Inception) to September 30, 2008
	2008	2007	
Cash paid for interest, net of amounts capitalized	\$ 6,104	\$ 38,242	\$ 99,746
Construction-in-process and debt issuance additions funded with accrued liabilities	\$ 43,406	\$ 47,227	\$ 43,406

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**Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS  
INFORMATION REGARDING FORWARD-LOOKING STATEMENTS**

This quarterly report contains certain statements that are, or may be deemed to be, forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the Securities Act), and Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act). All statements, other than statements of historical fact, included herein are forward-looking statements. Included among forward-looking statements are, among other things:

statements regarding our ability to pay distributions to our unitholders;

statements relating to the construction and operation of the Sabine Pass liquefied natural gas (LNG) receiving terminal, including statements concerning the completion or expansion thereof by certain dates or at all, the costs related thereto and certain characteristics, including amounts of regasification and storage capacity, the number of storage tanks and docks;

statements relating to the construction and operation of facilities related to the Sabine Pass LNG receiving terminal;

statements regarding our expected receipt of cash distributions from Sabine Pass LNG, L.P. (Sabine Pass LNG);

statements regarding any financing transactions or arrangements, or ability to enter into such transactions or arrangements;

statements regarding any terminal use agreement (TUA) or other commercial arrangements presently contracted, optioned or marketed or potential arrangements to be performed substantially in the future, including any cash distributions and revenues anticipated to be received and the anticipated timing thereof, and statements regarding the amounts of total LNG regasification capacity that are, or may become, subject to TUAs or other contracts;

statements regarding counterparties to our TUAs, construction contracts and other contracts;

statements regarding any business strategies, any business plans or any other plans, forecasts, projections or objectives, any or all of which are subject to change;

statements regarding conflicts of interest with Cheniere Energy, Inc. (Cheniere Energy) and its affiliates;

statements regarding legislative, governmental, regulatory, administrative or other public body actions, requirements, permits, investigations, proceedings or decisions; and

any other statements that relate to non-historical or future information.

These forward-looking statements are often identified by the use of terms such as achieve, anticipate, believe, estimate, expect, forecast, potential, project, propose, strategy and similar terms. Although we believe that the expectations reflected in these forward-looking statements are reasonable, they involve assumptions, risks and uncertainties, and these expectations may prove to be incorrect. You should not place undue reliance on these forward-looking statements, which speak only as of the date of this quarterly report.

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As used herein, the terms Cheniere Partners, we, our and us refer to Cheniere Energy Partners, L.P. and its wholly-owned subsidiaries effective March 26, 2007 upon the closing of its initial public offering, and to certain entities under common control prior to March 26, 2007, unless otherwise stated or indicated by context.

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Our actual results could differ materially from those anticipated in these forward-looking statements as a result of a variety of factors, including those discussed under **Risk Factors** in our annual report on Form 10-K for the year ended December 31, 2007. All forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by these risk factors. Other than as required under the securities laws, we assume no obligation to update or revise these forward-looking statements or provide reasons why actual results may differ.

The following discussion and analysis presents management's view of our business, financial condition and overall performance and should be read in conjunction with our Consolidated Combined Financial Statements and the accompanying notes in Item 1. Consolidated Financial Statements. This information is intended to provide investors with an understanding of our past performance, current financial condition and outlook for the future.

### **OVERVIEW**

Through our wholly-owned subsidiary, Sabine Pass LNG, we own and operate the Sabine Pass LNG receiving terminal currently under construction in western Cameron Parish, Louisiana on the Sabine Pass Channel. We are a development stage company without any revenues, operating cash flows and operating history as of September 30, 2008. Upon commencement of commercial operations in October 2008, we were entitled to begin receiving \$5.0 million per month of capacity reservation fee payments from Cheniere Marketing, LLC (Cheniere Marketing), formerly Cheniere Marketing, Inc., a wholly-owned subsidiary of Cheniere Energy, under its TUA with Sabine Pass LNG. As of September 30, 2008, Cheniere Marketing had prepaid capacity reservation fee payments to Sabine Pass LNG of \$15.0 million for the last three months of 2008.

We have completed physical construction of the initial 2.6 Bcf/d of sendout capacity and 10.1 Bcf of storage capacity at the Sabine Pass LNG receiving terminal and are now able to accept commercial cargoes. In order to complete commissioning and testing of this initial phase of the facility, our primary construction contractor, Bechtel Corporation, or Bechtel, will need to complete specified outstanding work items and we may need to obtain and process additional LNG. Construction of the remaining 1.4 Bcf/d of sendout capacity and 6.7 Bcf of storage capacity was approximately 84% complete as of September 30, 2008, and we anticipate achieving full operability, with total sendout capacity of approximately 4.0 Bcf/d and storage capacity of approximately 16.8 Bcf, during the third quarter of 2009.

We will contemplate making a final investment decision to commence construction of the Cheniere Southern Trail Pipeline upon, among other things, entering into acceptable commercial arrangements, receiving the Federal Energy Regulatory Commission's authorization to construct and operate the pipeline and obtaining adequate financing to construct the Cheniere Southern Trail Pipeline.

### **LIQUIDITY AND CAPITAL RESOURCES**

#### **Construction Costs**

Our estimated aggregate construction, commissioning and operating cost budget through the achievement of full operability of the Sabine Pass LNG receiving terminal, with approximately 4.0 Bcf/d of total sendout capacity and five storage tanks with approximately 16.8 Bcf of aggregate storage capacity, is approximately \$1,559 million, excluding financing costs. Of this amount, \$1,385.1 million of construction and commissioning costs had been incurred as of September 30, 2008. Our remaining construction, commissioning and operating costs are anticipated to be funded from restricted cash and cash equivalents designated for construction and working capital.

In September 2008, Hurricane Ike and related storm activity, such as windstorms, storm surges, and floods struck the Texas and Louisiana coast. We experienced minor damage at the Sabine Pass LNG receiving terminal

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with most of the damage impacting equipment and facilities associated with the 1.4 Bcf/d of sendout capacity and 6.7 Bcf of storage capacity still under construction. Impact to operations and the equipment and facilities associated with the initial 2.6 Bcf/d of sendout capacity and 10.1 Bcf of storage capacity was minimal. We continue to expect to complete construction of the remaining 1.4 Bcf/d of sendout capacity and 6.7 Bcf of storage capacity in the third quarter of 2009. Estimated costs to repair damage caused by Hurricane Ike are approximately \$38 million, of which we believe approximately \$28 million will be recoverable from insurance proceeds and other reimbursements.

### **TUA Revenues**

The entire 4.0 Bcf/d of regasification capacity that will be available at the Sabine Pass LNG receiving terminal upon completion of construction has been fully reserved under three long-term TUAs, under which Sabine Pass LNG's customers are required to pay fixed monthly fees, whether or not they use the terminal. We have achieved commercial operations completion so that capacity reservation fee TUA payments will begin to be made by these customers as follows:

Total LNG USA, Inc. ( Total ) has reserved approximately 1.0 Bcf/d of regasification capacity and has agreed to make monthly capacity payments to Sabine Pass LNG aggregating approximately \$125 million per year for 20 years commencing April 1, 2009. Total, S.A. has guaranteed Total's obligations under its TUA up to \$2.5 billion, subject to certain exceptions;

Chevron U.S.A., Inc. ( Chevron ) has reserved approximately 1.0 Bcf/d of regasification capacity and has agreed to make monthly capacity payments to Sabine Pass LNG aggregating approximately \$125 million per year for 20 years commencing not later than July 1, 2009. Chevron Corporation has guaranteed Chevron's obligations under its TUA up to 80% of the fees payable by Chevron; and

Cheniere Marketing has reserved the remaining 2.0 Bcf/d of regasification capacity, and is entitled to use any capacity not utilized by Total and Chevron. Cheniere Marketing has agreed to make monthly capacity payments aggregating approximately \$250 million per year through at least the third quarter of 2028, plus capacity payments of \$5 million per month for the three months beginning October 1, 2008 when the Sabine Pass LNG receiving terminal achieved commercial operations. Cheniere Energy has guaranteed Cheniere Marketing's obligations under its TUA.

Cheniere Marketing has a limited operating history, limited capital, and no credit rating. Cheniere Energy, which has guaranteed the obligations of Cheniere Marketing under its TUA, has a non-investment grade corporate rating. In addition, the LNG and natural gas marketing business activities of Cheniere Marketing have recently been downsized. If Cheniere Energy and its subsidiaries do not have sufficient liquidity to pay their obligations, including payments to Sabine Pass LNG required under the Cheniere Marketing TUA, then Sabine Pass LNG will likely be unable to make restricted cash distributions to us under the indenture governing the Sabine Pass LNG notes. If Sabine Pass LNG is unable to make such restricted cash distributions, then we will likely be unable to make our anticipated future quarterly cash distributions on our units. Under such circumstances and absent funding of the reserve account described in the paragraph that follows, Cheniere Marketing and Cheniere Energy would likely be unable to meet their TUA and guarantee obligations to Sabine Pass LNG.

In August 2008, Cheniere Common Units Holding, LLC, a subsidiary of Cheniere Energy, closed a \$250 million senior secured convertible term loan agreement ( 2008 Convertible Loans ). Proceeds of the 2008 Convertible Loans were used, among other purposes, to fund a reserve account for payments by Cheniere Marketing under its TUA.

### **Available Cash**

As of September 30, 2008, we had \$11,000 in cash and cash equivalents. In addition, we had \$450.7 million in restricted cash and cash equivalents and U.S. treasury securities, which were designated for the following purposes: \$164.4 million held by Sabine Pass LNG for working capital; \$105.6 million for construction costs of

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the Sabine Pass LNG receiving terminal; \$137.3 million for interest payments related to the Sabine Pass LNG notes described below; and \$43.4 million for cash distributions through the distribution made in respect of the quarter ending June 2009 to our common unitholders and related distributions to our general partner.

The foregoing reserved funds are anticipated to be sufficient to fund our construction budget, operating expenditures and interest requirements through the achievement of full operability of the Sabine Pass LNG receiving terminal in the third quarter of 2009. Regardless of whether we receive revenues from Cheniere Marketing under its TUA (or Cheniere Energy, on its guarantee), we thereafter expect to have sufficient cash flow from payments received under the Total and Chevron TUAs to meet our future operating expenditures, debt service requirements and, subject to declaration by our board of directors, distributions on all of our common and general partner units; however, if Sabine Pass LNG does not receive revenues from Cheniere Marketing's TUA or a replacement revenue source after June 30, 2009, the fixed charge coverage ratio test under the Sabine Pass LNG notes indenture will not be satisfied. Until the fixed charge coverage ratio test for a given quarter is met, Sabine Pass LNG will not be permitted to make distributions to us and we will not be able to make corresponding distributions to our unitholders. During any period when Sabine Pass LNG is not permitted to make distributions to us, our common unitholders will be entitled to accrue any distribution arrearages owed on their common units, which will be distributable to them once the fixed charge coverage ratio test is satisfied and we receive cash from Sabine Pass LNG.

### **Future Uses of Cash**

#### ***Sabine Pass LNG Notes***

Interest payments of approximately \$82.4 million are due on May 30 and November 30 of each year on the \$2,215.5 million of Sabine Pass LNG senior secured notes, consisting of \$550.0 million of 7<sup>1</sup>/<sub>4</sub>% Senior Secured Notes due 2013 and \$1,665.5 million of 7<sup>1</sup>/<sub>2</sub>% Senior Secured Notes due 2016. Under the indenture governing the Sabine Pass LNG notes, except for permitted tax distributions, Sabine Pass LNG may not make distributions until certain conditions are satisfied. The indenture requires that Sabine Pass LNG apply its net operating cash flow (i) first, to fund with monthly deposits its next semiannual payment of approximately \$82.4 million of interest on the Sabine Pass LNG notes, and (ii) second, to fund a one-time, permanent debt service reserve fund equal to one semiannual interest payment of approximately \$82.4 million on the Sabine Pass LNG notes. Distributions will be permitted only after satisfaction of the foregoing funding requirements, after satisfying a fixed charge coverage ratio test of 2:1 and after satisfying other conditions specified in the indenture.

#### ***Cash Distributions to Unitholders***

For each calendar quarter through June 30, 2009, we will make quarterly cash distributions of \$0.425 per unit on all outstanding common units, as well as related distributions to our general partner, using cash from a \$98.4 million distribution reserve funded with proceeds from our initial public offering and held as restricted cash and cash equivalents. Beginning with the quarter ending September 30, 2009, we intend to pay distributions to our unitholders primarily from operating cash flows, subject to satisfying the fixed charge coverage ratio test of 2:1 described above. After payment of the distributions with respect to the nine months ended September 30, 2008, \$43.4 million remained in the distribution reserve.

#### ***Services Agreements***

In February 2005, Sabine Pass LNG entered into a 20-year operation and maintenance agreement with a wholly-owned subsidiary of Cheniere Energy pursuant to which we receive all necessary services required to construct, operate and maintain the Sabine Pass LNG receiving terminal. Prior to substantial completion of the Sabine Pass LNG receiving terminal, Sabine Pass LNG is required to pay a fixed monthly fee of \$95,000 (indexed for inflation beginning in 2010) under the agreement. The fixed monthly fee will increase to \$130,000 (indexed for inflation beginning in 2010) upon substantial completion of Sabine Pass LNG's EPC contract with



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Bechtel, and the counterparty will thereafter be entitled to a bonus equal to 50% of the salary component of labor costs in certain circumstances to be agreed upon between Sabine Pass LNG and the counterparty at the beginning of each operating year. In addition, Sabine Pass LNG is required to reimburse the counterparty for its operating expenses, which are comprised primarily of labor expenses.

In February 2005, Sabine Pass LNG entered into a 20-year management services agreement with its general partner, which is a wholly-owned subsidiary of us, pursuant to which its general partner was appointed to manage the construction and operation of the Sabine Pass LNG receiving terminal, excluding those matters provided for under the operation and maintenance agreement described in the paragraph above. In August 2008, the general partner of Sabine Pass LNG assigned all of its rights and obligations under the management services agreement to Cheniere LNG Terminals, Inc. (Cheniere Terminals), a wholly-owned subsidiary of Cheniere Energy. Prior to substantial completion of the Sabine Pass LNG receiving terminal, Sabine Pass LNG is required to pay Cheniere Terminals a monthly fixed fee of \$340,000 (indexed for inflation beginning in 2010); thereafter, the monthly fixed fee will increase to \$520,000 (indexed for inflation beginning in 2010).

We entered into a services agreement with Cheniere Terminals pursuant to which we will pay Cheniere Terminals an annual administrative fee of \$10 million (adjusted for inflation after January 1, 2007) commencing January 1, 2009 for the provision of various general and administrative services for our benefit following the closing of our initial public offering. In addition, we will reimburse Cheniere Terminals for its services in an amount equal to the sum of all out-of-pocket costs and expenses incurred by Cheniere Terminals that are directly related to our business or activities.

During the three and nine months ended September 30, 2008, we paid an aggregate of \$1.3 million and \$3.9 million, respectively, under the foregoing services agreement from restricted cash and cash equivalents. For the period from October 20, 2003 (date of inception) to September 30, 2008, we paid \$18.3 million. Until substantial completion of the Sabine Pass LNG receiving terminal and revenues are received under the TUAs, we anticipate continuing to utilize restricted cash and cash equivalents to satisfy our obligations under these service agreements.

### ***Long-Term Note Affiliate***

In March 2007, we entered into a \$12.0 million unsecured revolving credit note with Cheniere LNG Financial Services, Inc., a wholly-owned subsidiary of Cheniere Energy, to be paid upon demand but no sooner than January 1, 2010, or the date on which we have sufficient available cash. The purpose of this note is to provide funds for the payment of certain public company and other expenses that cannot be funded with proceeds from the Sabine Pass LNG notes. Borrowings under this note bear interest at a fixed 7.50% rate with unpaid interest compounded semi-annually. The outstanding principal plus interest as of September 30, 2008 was \$2.1 million.

### ***State Tax Sharing Agreement***

In November 2006, Sabine Pass LNG entered into a state tax sharing agreement with Cheniere Energy. Under this agreement, Cheniere Energy has agreed to prepare and file all Texas franchise tax returns which it and Sabine Pass LNG are required to file on a combined basis and to timely pay the combined tax liability. If Cheniere Energy, in its sole discretion, demands payment, Sabine Pass LNG will pay to Cheniere Energy an amount equal to the Texas franchise tax that Sabine Pass LNG would be required to pay if its Texas franchise tax liability were computed on a separate company basis. This agreement contains similar provisions for other state and local taxes that Cheniere Energy and Sabine Pass LNG are required to file on a combined, consolidated or unitary basis. The agreement is effective for tax returns first due on or after January 1, 2008. We do not expect to make any tax payments under this agreement for 2008.

**Index to Financial Statements****Historical Sources and Uses of Cash**

The following table summarizes the sources and uses of our cash and cash equivalents for the nine months ended September 30, 2007 and 2008, and the period from October 20, 2003 (date of inception) to September 30, 2008. The table presents capital expenditures on a cash basis; therefore, these amounts differ from the amounts of capital expenditures, including accruals, that are referred to elsewhere in this document. Additional discussion of these items follows the table (in thousands):

	Nine Months Ended September 30,		Period from October 20, 2003 (Date of Inception) to September 30, 2008
	2008	2007	
<b>SOURCES OF CASH AND CASH EQUIVALENTS</b>			
Use of restricted cash and cash equivalents	\$ 357,520	\$ 332,142	\$
Borrowings from debt	144,965		2,560,365
Capital contribution by partner			161,572
Proceeds from issuance of common units in partnership		98,442	98,442
Affiliate payable	1		35,117
Borrowings from debt affiliate	1,472	282	2,117
Proceeds from subordinated note affiliate			37,377
<b>Total sources of cash and cash equivalents</b>	<b>503,958</b>	<b>430,866</b>	<b>2,894,990</b>
<b>USES OF CASH AND CASH EQUIVALENTS</b>			
LNG receiving terminal construction-in-process, net	(333,848)	(307,066)	(1,389,137)
Advances to affiliate LNG held for commissioning, net of amounts transferred to LNG terminal construction-in-process	(16,595)		(16,595)
Investment in restricted cash and cash equivalents	(106,012)	(977)	(446,667)
Investment in restricted treasury securities		(75,023)	(63,923)
Operating cash flow	(1,474)	(278)	(415)
Repayment of debt			(383,400)
Repayment of subordinated note affiliate			(37,377)
Distributions to owners	(34,368)	(12,213)	(436,385)
Debt issuance costs	(4,586)	(740)	(66,371)
Advances under long-term contracts	(7,077)	(34,567)	(52,713)
Other			(1,996)
<b>Total uses of cash and cash equivalents</b>	<b>(503,960)</b>	<b>(430,864)</b>	<b>(2,894,979)</b>
<b>Net increase (decrease) in cash and cash equivalents</b>	<b>\$ (2)</b>	<b>\$ 2</b>	<b>\$ 11</b>
<b>Cash and cash equivalents at end of period</b>	<b>\$ 11</b>	<b>\$ 9</b>	<b>\$ 11</b>

*Use of restricted cash and cash equivalents*

Under the indenture governing the Sabine Pass LNG notes, a portion of the proceeds from the Sabine Pass LNG notes are required to be used for scheduled interest payments through May 2009 and to fund the cost to complete construction of the Sabine Pass LNG receiving terminal. Due to these restrictions imposed by the indenture, the proceeds are not presented as cash and cash equivalents. Therefore, when proceeds from the Sabine Pass LNG notes are used, they are presented as a source of cash and cash equivalents. In the nine months ended September 30, 2008 and 2007, the \$357.5 million and \$332.1 million, respectively, of restricted cash and cash equivalents were primarily used to pay for construction activities at the Sabine Pass LNG receiving terminal.

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*Borrowings from debt*

Borrowings from debt were \$145.0 million, zero and \$2,560.4 million in the nine months ended September 30, 2008 and 2007, and the period from October 20, 2003 (inception) to September 30, 2008, respectively. The \$145.0 million borrowings from debt during the nine months ended September 30, 2008, relates to the additional issuance of Senior Notes due 2016, net of discount.

*LNG receiving terminal construction-in-process, net*

Capital expenditures for the Sabine Pass LNG receiving terminal were \$333.8 million, \$307.1 million and \$1,389.1 million in the nine months ended September 30, 2008 and 2007, and the period from October 20, 2003 (inception) to September 30, 2008, respectively. Our capital expenditures increased in the nine months ended September 30, 2008 compared to the nine months ended September 30, 2007 as a result of the commissioning process at the Sabine Pass LNG receiving terminal.

*Advances to affiliate LNG held for commissioning, net of amounts transferred to LNG receiving terminal construction-in-process*

During the nine months ended September 30, 2008, we advanced Cheniere Marketing \$16.6 million for the purchase of LNG for commissioning, net of amounts transferred to LNG receiving terminal construction-in-process.

*Investment in restricted cash and cash equivalents*

During the nine months ended September 30, 2008, Sabine Pass LNG invested \$100.0 million of the \$145.0 million of net proceeds from the additional issuance of the 2016 Notes into a construction account to pay construction expenses of cost overruns related to the construction, cool down, commissioning and completion of the Sabine Pass LNG receiving terminal.

*Advances under long-term contracts*

Advances under long-term contracts decreased in the nine months ended September 30, 2008 compared to the nine months ended September 30, 2007 as a result of us nearing construction completion of the initial send out capacity of approximately 2.6 Bcf/d and storage capacity of approximately 10.1 Bcf at the Sabine Pass LNG receiving terminal. During the nine months ended September 30, 2008, the Sabine Pass LNG receiving terminal received equipment that Sabine Pass LNG had previously advanced payment for under long-term contracts.

**Off-Balance Sheet Arrangements**

As of September 30, 2008, we had no off-balance sheet arrangements that may have a current or future material affect on our financial position or results of operations.

**RESULTS OF OPERATIONS**

**Three Months Ended September 30, 2008 vs. Three Months Ended September 30, 2007**

*Overall Operations*

Our net loss was \$10.9 million in the three months ended September 30, 2008, or a 2% decrease from our net loss in the three months ended September 30, 2007. The \$0.2 million decrease in the net loss was primarily due to a gain on derivatives and decreased interest expense, which were partially offset by decreased interest income, increased LNG receiving terminal repair and maintenance expense and increased depreciation expense.

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### ***Derivative Gain***

During the three months ended September 30, 2008, we recognized a \$14.7 million derivative gain. On behalf of Sabine Pass LNG, Cheniere Marketing entered into natural gas swaps to hedge the exposure to variability in expected future cash flows from sales of excess LNG purchased for commissioning and performance testing during the three months ended September 30, 2008.

### ***Interest Expense, net***

Interest expense, net of amounts capitalized, decreased \$2.8 million in the three months ended September 30, 2008 compared to the three months ended September 30, 2007. This decrease in interest expense primarily resulted from an increase in construction costs and consequently an increase in capitalized interest in the three months ended September 30, 2008 compared to the three months ended September 30, 2007.

### ***Interest Income***

Interest income decreased \$10.5 million in the three months ended September 30, 2008 compared to the three months ended September 30, 2007. This decrease was a result of less restricted cash and cash equivalents being invested during the three months ended September 30, 2008 compared to the three months ended September 30, 2007.

### ***LNG receiving terminal repair and maintenance expense***

LNG receiving terminal repair and maintenance expense increased \$2.8 million in the three months ended September 30, 2008 compared to the three months ended September 30, 2007. This increase relates to part of the damage caused by Hurricane Ike to the Sabine Pass LNG receiving terminal's initial 2.6 Bcf/d of regassification capacity and the 10.1 Bcf of storage capacity placed into service in the third quarter of 2008.

### ***Depreciation expense***

Depreciation expense increased \$1.8 million in the three months ended September 30, 2008 compared to the three months ended September 30, 2007. This increase resulted from our having begun depreciating the Sabine Pass LNG receiving terminal's initial 2.6 Bcf/d of regassification capacity and 10.1 Bcf of storage capacity commencing in the third quarter of 2008 when it was ready for use and placed in service.

## **Nine Months Ended September 30, 2008 vs. Nine Months Ended September 30, 2007**

### ***Overall Operations***

Our net loss was \$49.9 million in the nine months ended September 30, 2008, a 39% increase from our net loss in the nine months ended September 30, 2007. The \$14.0 million increase in the net loss was primarily due to decreased interest income, increased LNG receiving terminal repair and maintenance expense, increased labor and overhead charge from affiliate and increased depreciation expense, which were partially offset by decreased interest expense and derivative gain.

### ***Interest Income***

Interest income decreased \$29.8 million in the nine months ended September 30, 2008 compared to the nine months ended September 30, 2007. This decrease was a result of less restricted cash and cash equivalents being invested during the nine months ended September 30, 2008 compared to the nine months ended September 30, 2007.

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***LNG receiving terminal repair and maintenance expense***

LNG receiving terminal repair and maintenance expense increased \$2.8 million in the nine months ended September 30, 2008 compared to the nine months ended September 30, 2007. This increase relates to part of the damage caused by Hurricane Ike to the Sabine Pass LNG receiving terminal's initial 2.6 Bcf/d of regassification capacity and 10.1 Bcf of storage capacity placed into service in the third quarter of 2008.

***Labor and overhead charge from affiliate***

Labor and overhead charge from affiliate increased \$1.9 million in the nine months ended September 30, 2008 compared to the nine months ended September 30, 2007. This increase was a result of increased training and development costs and decreased capitalized labor and overhead charge from affiliate associated with the commencement of commercial operations in the third quarter of 2008.

***Depreciation expense***

Depreciation expense increased \$1.8 million in the nine months ended September 30, 2008 compared to the nine months ended September 30, 2007. This increase resulted from our placing into service and beginning to depreciate the initial 2.6 Bcf/d of sendout capacity and 10.1 Bcf of storage capacity of the Sabine Pass LNG receiving terminal in the third quarter of 2008.

***Interest Expense, net***

Interest expense, net of amounts capitalized, decreased \$22.4 million in the nine months ended September 30, 2008 compared to the nine months ended September 30, 2007. This decrease in interest expense primarily resulted from an increase in construction costs and consequently an increase in capitalized interest in the nine months ended September 30, 2008 compared to the nine months ended September 30, 2007.

***Derivative Gain***

During the nine months ended September 30, 2008, we recognized a \$2.3 million derivative gain. On behalf of Sabine Pass LNG, Cheniere Marketing entered into natural gas swaps to hedge the exposure to variability in expected future cash flows from sales of excess LNG purchased for commissioning and performance testing during the nine months ended September 30, 2008.

**OTHER MATTERS**

**Critical Accounting Estimates and Policies**

The selection and application of accounting policies is an important process that has developed as our business activities have evolved and as the accounting rules have developed. Accounting rules generally do not involve a selection among alternatives but involve an implementation and interpretation of existing rules, and the use of judgment, to the specific set of circumstances existing in our business. In preparing our financial statements in conformity with U.S. generally accepted accounting principles ( GAAP ), we make every effort to comply properly with all applicable rules on or before their adoption, and we believe that the proper implementation and consistent application of the accounting rules are critical. However, not all situations are specifically addressed in the accounting literature. In these cases, we must use our best judgment to adopt a policy for accounting for these situations. We accomplish this by analogizing to similar situations and the accounting guidance governing them.

***Accounting for LNG Activities***

Generally, expenditures for direct construction activities, major renewals and betterments are capitalized, while expenditures for maintenance and repairs and general and administrative activities are charged to expense as incurred.

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Beginning in 2006, site rental costs have been expensed as required by Financial Accounting Standards Board ( FASB ) Staff Position 13-1, *Accounting for Rental Costs Incurred During a Construction Period*.

During the construction period of the Sabine Pass LNG receiving terminal, we capitalize interest and other related debt costs in accordance with Statement of Financial Accounting Standards ( SFAS ) No. 34, *Capitalization of Interest Cost*, as amended by SFAS No. 58, *Capitalization of Interest Cost in Financial Statements That Include Investments Accounted for by the Equity Method (an Amendment of FASB Statement No. 34)*. Upon commencement of operations, capitalized interest, as a component of the total cost, will be amortized over the estimated useful life of the asset.

In connection with the construction of the Sabine Pass LNG receiving terminal, we require LNG to perform certain commissioning activities, as follows:

**Cool down** A minimum amount of LNG will be used to cool down the LNG receiving terminal. Cool down represents the amount of LNG required to cool the LNG receiving terminal to its normal operating temperature.

**LNG heel** A certain amount of LNG will be used to establish a level of LNG inventory in each LNG storage tank and in the LNG receiving terminal piping in order for the LNG receiving terminal to function properly.

**Equipment commissioning** The remaining amount of the LNG will be used to commission the equipment in the LNG receiving terminal to ensure that it performs at designed specifications. Equipment commissioning will result in natural gas being sold. LNG purchased for commissioning activities is recorded at cost and classified as a non-current asset on our Consolidated Balance Sheets as LNG held for commissioning. As the LNG held for commissioning is used to cool down the LNG receiving terminal and establish LNG heel in the LNG receiving terminal, we capitalize the portion used. The LNG used in the commissioning process is capitalized net of amounts received from the sale of natural gas.

### ***Revenue Recognition***

LNG receiving terminal capacity reservation fees are recognized as revenue over the term of the respective TUAs. Advance capacity reservation fees are initially deferred and recognized as earned.

### ***Cash Flow Hedges***

We have used, and may in the future use, derivative instruments to limit our exposure to variability in expected future cash flows. As defined in SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, cash flow hedge transactions hedge the exposure to variability in expected future cash flows (i.e., in our case, the variability of floating interest rate exposure). In the case of cash flow hedges, the hedged item (the underlying risk) is generally unrecognized (i.e., not recorded on the balance sheet prior to settlement), and any changes in the fair value, therefore, will not be recorded within earnings. Conceptually, if a cash flow hedge is effective, this means that a variable, such as a movement in interest rates, has been effectively fixed so that any fluctuations will have no net result on either cash flows or earnings. Therefore, if the changes in fair value of the hedged item are not recorded in earnings, then the changes in fair value of the hedging instrument (the derivative) must also be excluded from the income statement or else a one-sided net impact on earnings will be reported, despite the fact that the establishment of the effective hedge results in no net economic impact. To prevent such a scenario from occurring, SFAS No. 133 requires that the fair value of a derivative instrument designated as a cash flow hedge be recorded as an asset or liability on the balance sheet, but with the offset reported as part of other comprehensive income, to the extent that the hedge is effective. We assess, both at the inception of each hedge and on an on-going basis, whether the derivatives that are used in our hedging transactions are highly effective in offsetting changes in cash flows of the hedged items. On an on-going basis,

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we monitor the actual dollar offset of the hedges' market values compared to hypothetical cash flow hedges. Any ineffective portion of the cash flow hedges will be reflected in earnings. Ineffectiveness is the amount of gains or losses from derivative instruments that are not offset by corresponding and opposite gains or losses on the expected future transaction.

### **New Accounting Pronouncements**

On January 1, 2008, we adopted SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities including an amendment of FASB Statement No. 115* ( SFAS 159 ). SFAS 159 permits entities to choose to measure many financial instruments and certain other assets and liabilities at fair value on an instrument-by-instrument basis (the fair value option) with changes in fair value reported in earnings. We recorded our derivative contracts at fair value in accordance with SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, as amended ( SFAS 133 ). The adoption of SFAS 159 had no impact on the Consolidated Combined Financial Statements, as management did not elect the fair value option for any financial instruments or other assets and liabilities.

On January 1, 2008, we adopted SFAS No. 157, *Fair Value Measurements* ( SFAS 157 ) as it relates to financial assets and financial liabilities. In February 2008, the Financial Accounting Standards Board ( FASB ) issued FASB Staff Position ( FSP ) No. FAS 157-2, *Effective Date of FASB Statement No. 157*, which delayed the effective date of SFAS 157 for all nonfinancial assets and nonfinancial liabilities, except those that are recognized or disclosed at fair value in the financial statements on at least an annual basis, until January 1, 2009 for calendar year-end entities. The adoption of SFAS 157 did not have a material impact on our Consolidated Combined Financial Statements.

In March 2008, the FASB issued SFAS No. 161, *Disclosures about Derivative Instruments and Hedging Activities an amendment of FASB Statement No. 133* ( SFAS 161 ). SFAS 161 requires enhanced disclosures about an entity's derivative and hedging activities, including (i) how and why an entity uses derivative instruments, (ii) how derivative instruments and related hedged items are accounted for under SFAS 133, and (iii) how derivative instruments and related hedged items affect an entity's financial position, financial performance, and cash flows. This standard becomes effective for us on January 1, 2009. Earlier adoption of SFAS 161 and, separately, comparative disclosures for earlier periods at initial adoption are encouraged. As SFAS 161 only requires enhanced disclosures, this standard will have no impact on our Consolidated Combined Financial Statements.

In April 2008, the FASB issued FSP FAS No. 142-3, *Determination of the Useful Life of Intangible Assets* ( FSP FAS 142-3 ). This FSP amends the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset under FASB Statement No. 142, *Goodwill and Other Intangible Assets* ( SFAS 142 ). The intent of this FSP is to improve the consistency between the useful life of a recognized intangible asset under SFAS 142 and the period of expected cash flows used to measure the fair value of the asset under SFAS No. 141R, and other GAAP. This FSP is effective for financial statements issued for fiscal years beginning after December 15, 2008, and interim periods within those fiscal years. Early adoption is prohibited. We are currently evaluating the impact of FSP FAS 142-3 but do not expect the adoption of this pronouncement will have a material impact on our Consolidated Combined Financial Statements.

In May 2008, the FASB issued SFAS No. 162, *The Hierarchy of Generally Accepted Accounting Principles* ( SFAS 162 ). SFAS 162 identifies the sources of accounting principles and the framework for selecting principles to be used in the preparation of financial statements of nongovernmental entities that are presented in conformity with GAAP. This statement will be effective 60 days following the SEC's approval of the Public Company Accounting Oversight Board's amendments to AU section 411, *The Meaning of Present Fairly in Conformity with Generally Accepted Accounting Principles*. We are currently evaluating the impact of SFAS 162 but do not expect the adoption of this pronouncement will have a material impact on our Consolidated Combined Financial Statements.

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**Item 3. Quantitative and Qualitative Disclosures About Market Risk**  
**Cash Investments**

We have cash investments that we manage based on internal investment guidelines that emphasize liquidity and preservation of capital. Such cash investments are stated at historical cost, which approximates fair market value on our Consolidated Balance Sheets.

**Sabine Pass LNG Derivative Commodity Price Risk**

On behalf of Sabine Pass LNG, Cheniere Marketing entered into natural gas NYMEX swaps accounted for as derivatives. The NYMEX swaps were entered into to hedge the exposure to variability in expected future cash flows related to commissioning cargoes purchased by Cheniere Marketing in the second quarter of 2008 that are expected to be sold as part of the testing phase of the commissioning process. As of September 30, 2008, Cheniere Marketing on behalf of Sabine Pass LNG had entered into a total of 1,292,500 MMBtu of NYMEX swaps through February 2009 with one counterparty for which it will receive fixed prices of \$8.44 to \$12.59 per MMBtu. At September 30, 2008, the value of the derivatives was an asset of \$3.8 million.

**Item 4. Disclosure Controls and Procedures**

We maintain a set of disclosure controls and procedures that are designed to ensure that information required to be disclosed by us in the reports filed by us under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. As of the end of the period covered by this report, we evaluated, under the supervision and with the participation of our general partner's management, including our general partner's Chief Executive Officer and Chief Financial Officer, the effectiveness of our disclosure controls and procedures pursuant to Rule 13a-15 of the Exchange Act. Based on that evaluation, our general partner's Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures are effective.

During the most recent fiscal quarter, there have been no changes in our internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.



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In the future, we may be involved as a party to various legal proceedings, which are incidental to the ordinary course of business. We regularly analyze current information and, as necessary, provide accruals for probable liabilities on the eventual disposition of these matters. In the opinion of management of our general partner and legal counsel, as of September 30, 2008, there were no known threatened or pending legal matters that could reasonably be expected to have a material adverse impact on our consolidated combined results of operations, financial position or cash flows.

**Item 6. Exhibits**

(a) Each of the following exhibits is filed herewith:

- 10.1 Assignment, Assumption, Consent and Release Agreement of Management Services Agreement, dated August 15, 2008, between Sabine Pass LNG-GP, Inc. and Cheniere LNG Terminals, Inc. (Incorporated by reference to Exhibit 10.1 to Cheniere Energy, Inc. s Quarterly Report on Form 10-Q (SEC File No. 001-16383), for the quarter ended September 30, 2008)
- 10.2 CQP GP Consent and Agreement (Operation and Maintenance Agreement), dated August 15, 2008, among Cheniere LNG O&M Services, LLC, Cheniere Energy Partners GP, LLC and Bank of New York Mellon. (Incorporated by reference to Exhibit 10.2 to Cheniere Energy, Inc. s Quarterly Report on Form 10-Q (SEC File No. 001-16383), for the quarter ended September 30, 2008)
- 10.3 CQP Consent and Agreement (Management and Administrative Services Letter Agreement) among Cheniere LNG Terminals, Inc., Cheniere Energy Partners, L.P. and Bank of New York Mellon. (Incorporated by reference to Exhibit 10.3 to Cheniere Energy, Inc. s Quarterly Report on Form 10-Q (SEC File No. 001-16383), for the quarter ended September 30, 2008)
- 10.4 Sabine Consent and Agreement (Operation and Maintenance Agreement), dated August 15, 2008, among Cheniere Energy Partners GP, LLC, Sabine Pass LNG, L.P. and Bank of New York Mellon. (Incorporated by reference to Exhibit 10.4 to Cheniere Energy, Inc. s Quarterly Report on Form 10-Q (SEC File No. 001-16383), for the quarter ended September 30, 2008)
- 10.5 Sabine Consent and Agreement (Management Services Agreement), dated August 15, 2008, among Cheniere LNG Terminals, Inc., Sabine Pass LNG, L.P. and Bank of New York Mellon. (Incorporated by reference to Exhibit 10.5 to Cheniere Energy, Inc. s Quarterly Report on Form 10-Q (SEC File No. 001-16383), for the quarter ended September 30, 2008)
- 10.6 Change Order 10 to Agreement for Engineering, Procurement, Construction and Management of Construction Services for the Sabine Phase 2 Receiving, Storage and Regasification Terminal Expansion, dated July 21, 2006, between Sabine Pass LNG, L.P. and Bechtel Corporation. (Incorporated by reference to Exhibit 10.8 to Cheniere Energy, Inc. s Quarterly Report on Form 10-Q (SEC File No. 001-16383), for the quarter ended September 30, 2008)
- 10.7 Amendment to Agreement, dated September 3, 2008, for modification for transfer of risk of loss and modification of certain other obligations between Owner and Contractor under the Lump Sum Turnkey Agreement for Engineering, Procurement and Construction of the Sabine Pass LNG Receiving, Storage and Regasification Terminal by and between Sabine Pass LNG, L.P. and Bechtel Corporation, dated December 18, 2004. (Incorporated by reference to Exhibit 10.9 to Cheniere Energy, Inc. s Quarterly Report on Form 10-Q (SEC File No. 001-16383), filed on November 6, 2008)
- 31.1 Certification by Chief Executive Officer required by Rule 13a-14(a) and 15d-14(a) under the Exchange Act
- 31.2 Certification by Chief Financial Officer required by Rule 13a-14(a) and 15d-14(a) under the Exchange Act
- 32.1 Certification by Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 32.2 Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002



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**SIGNATURES**

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

CHENIERE ENERGY PARTNERS, L.P.

By: Cheniere Energy Partners GP, LLC,

its general partner

/s/ Jerry D. Smith  
Jerry D. Smith

Chief Accounting Officer (on behalf of the  
registrant and as principal accounting officer)

Date: November 6, 2008