

USA Compression Partners, LP  
Form 10-Q  
August 04, 2016  
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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

Form 10-Q

(MARK ONE)

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

FOR THE QUARTERLY PERIOD ENDED June 30, 2016

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. 001-35779

USA Compression Partners, LP

(Exact name of registrant as specified in its charter)

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Delaware (State or Other Jurisdiction of Incorporation or Organization)	75-2771546 (I.R.S. Employer Identification No.)
100 Congress Avenue, Suite 450 Austin, Texas (Address of principal executive offices)	78701 (Zip Code)

(512) 473-2662

(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 has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). 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 the definitions 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

As of August 2, 2016, there were 54,866,123 common units outstanding.



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## PART I. FINANCIAL INFORMATION

## ITEM 1. Financial Statements

## USA COMPRESSION PARTNERS, LP AND SUBSIDIARIES

## Unaudited Condensed Consolidated Balance Sheets

(Dollars in thousands, except unit amounts)

	June 30, 2016	December 31, 2015
Assets		
Current assets:		
Cash and cash equivalents	\$ 7	\$ 7
Accounts receivable, net:		
Trade, net	24,911	28,465
Other	3,153	3,023
Inventory, net	20,682	18,872
Prepaid expenses	2,872	2,600
Total current assets	51,625	52,967
Property and equipment, net	1,300,561	1,318,043
Installment receivable	15,707	17,275
Identifiable intangible assets, net	76,981	78,773
Goodwill	35,866	35,866
Other assets	7,842	6,847
Total assets	\$ 1,488,582	\$ 1,509,771
Liabilities and Partners' Capital		
Current liabilities:		
Accounts payable	\$ 16,421	\$ 23,840
Accrued liabilities	23,872	20,582
Deferred revenue	16,186	17,000
Total current liabilities	56,479	61,422
Long-term debt	735,120	729,187
Other liabilities	1,008	874
Partners' capital:		
Limited partner interest:		
Common units, 54,866,123 and 38,556,245 units issued and outstanding, respectively	686,717	557,583

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Subordinated units, 14,048,588 issued and outstanding at December 31, 2015	—	150,787
General partner's interest	9,258	9,918
Total partners' capital	695,975	718,288
Total liabilities and partners' capital	\$ 1,488,582	\$ 1,509,771

See accompanying notes to unaudited condensed consolidated financial statements.

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## USA COMPRESSION PARTNERS, LP AND SUBSIDIARIES

## Unaudited Condensed Consolidated Statements of Operations

(Dollars in thousands, except unit amounts)

	Three months ended June 30,		Six months ended June 30,	
	2016	2015	2016	2015
Revenues:				
Contract operations	\$ 62,785	\$ 65,552	\$ 127,063	\$ 129,587
Parts and service	726	838	2,815	1,803
Total revenues	63,511	66,390	129,878	131,390
Costs and expenses:				
Cost of operations, exclusive of depreciation and amortization	18,654	19,079	39,483	38,290
Selling, general and administrative	11,180	10,350	20,919	20,079
Depreciation and amortization	23,412	21,507	45,506	42,238
Loss (gain) on sale of assets	1,072	(23)	950	(218)
Impairment of compression equipment	693	26,829	693	26,829
Total costs and expenses	55,011	77,742	107,551	127,218
Operating income (loss)	8,500	(11,352)	22,327	4,172
Other income (expense):				
Interest expense, net	(5,139)	(4,415)	(10,201)	(8,409)
Other	7	5	14	10
Total other expense	(5,132)	(4,410)	(10,187)	(8,399)
Net income (loss) before income tax expense	3,368	(15,762)	12,140	(4,227)
Income tax expense (Note 6)	94	142	328	221
Net income (loss)	\$ 3,274	\$ (15,904)	\$ 11,812	\$ (4,448)
Net income (loss) allocated to:				
General partner's interest in net income (loss)	\$ 345	\$ (7)	\$ 753	\$ 362
Limited partners' interest in net income (loss):				
Common units	\$ 2,929	\$ (11,043)	\$ 13,770	\$ (3,225)
Subordinated units	\$ —	\$ (4,854)	\$ (2,711)	\$ (1,585)
Weighted average common units outstanding:				
Basic	54,505,856	32,449,180	50,305,065	32,072,282
Diluted	54,751,902	32,449,180	50,637,960	32,072,282
Weighted average subordinated units outstanding:				
Basic and diluted	—	14,048,588	3,550,742	14,048,588
Net income (loss) per common unit:				
Basic	\$ 0.05	\$ (0.34)	\$ 0.27	\$ (0.10)
Diluted	\$ 0.05	\$ (0.34)	\$ 0.27	\$ (0.10)
Net income (loss) per subordinated unit:				
Basic and diluted	\$ —	\$ (0.35)	\$ (0.76)	\$ (0.11)
	\$ 0.525	\$ 0.525	\$ 1.05	\$ 1.04

Distributions declared per limited partner unit for  
respective periods

See accompanying notes to unaudited condensed consolidated financial statements.

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## USA COMPRESSION PARTNERS, LP AND SUBSIDIARIES

## Unaudited Condensed Consolidated Statement of Changes in Partners' Capital

Six Months Ended June 30, 2016

(Dollars and units in thousands)

	Partners' Capital				General Partner Amount	Total Partners' Capital
	Common Units		Subordinated Units			
	Units	Amount	Units	Amount		
Partners' capital, December 31, 2015	38,556	\$ 557,583	14,049	\$ 150,787	\$ 9,918	\$ 718,288
Vesting of phantom units	191	1,456	—	—	—	1,456
Distributions and DERs	—	(48,704)	—	(7,376)	(1,413)	(57,493)
Issuance of common units	2,070	21,327	—	—	—	21,327
Unit-based compensation	—	585	—	—	—	585
Net income (loss)	—	13,770	—	(2,711)	753	11,812
Conversion of subordinated units to common units	14,049	140,700	(14,049)	(140,700)	—	—
Partners' capital, June 30, 2016	54,866	\$ 686,717	—	\$ —	\$ 9,258	\$ 695,975

See accompanying notes to unaudited condensed consolidated financial statements.

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## USA COMPRESSION PARTNERS, LP AND SUBSIDIARIES

## Unaudited Condensed Consolidated Statements of Cash Flows

(Dollars in thousands)

	Six months ended June 30,	
	2016	2015
Cash flows from operating activities:		
Net income (loss)	\$ 11,812	\$ (4,448)
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	45,506	42,238
Amortization of debt issue costs	1,015	870
Unit-based compensation expense	4,834	2,264
Net loss (gain) on sale of assets	950	(218)
Impairment of compression equipment	693	26,829
Changes in assets and liabilities:		
Accounts receivable	4,993	3,610
Inventory	(1,452)	(12,465)
Prepays	(272)	(1,273)
Other noncurrent assets	—	3
Accounts payable	(9,128)	(8,651)
Accrued liabilities and deferred revenue	(494)	(209)
Net cash provided by operating activities	58,457	48,550
Cash flows from investing activities:		
Capital expenditures	(24,810)	(182,687)
Proceeds from sale of property and equipment	166	129
Proceeds from insurance recovery	—	159
Net cash used in investing activities	(24,644)	(182,399)
Cash flows from financing activities:		
Proceeds from long-term debt	142,713	295,798
Payments on long-term debt	(136,780)	(137,651)
Net proceeds from issuance of common units	—	745
Cash paid for taxes related to net settlement of unit-based awards	(98)	(189)
Cash distributions	(37,638)	(21,467)
Financing costs	(2,010)	(3,386)
Net cash provided by (used in) financing activities	(33,813)	133,850
Increase in cash and cash equivalents	—	1
Cash and cash equivalents, beginning of period	7	6
Cash and cash equivalents, end of period	\$ 7	\$ 7
Supplemental cash flow information:		
Cash paid for interest	\$ 9,940	\$ 8,062

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Cash paid for taxes	\$ 265	\$ 299
Supplemental non-cash transactions:		
Non-cash distributions to certain limited partners (DRIP)	\$ 21,327	\$ 26,964
Change in capital expenditures included in accounts payable and accrued liabilities	\$ 3,616	\$ 13,783
Transfers to/from inventory to property and equipment	\$ 667	\$ 684
Transfer from long term installment receivable to short term	\$ (1,568)	\$ (1,455)

See accompanying notes to unaudited condensed consolidated financial statements.

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## USA COMPRESSION PARTNERS, LP AND SUBSIDIARIES

## NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

## (1) Organization and Summary of Significant Accounting Policies

## (a) Organization

USA Compression Partners, LP (the “Partnership”) is a publicly traded Delaware limited partnership formed to own its subsidiaries, through which it operates the business. The common units representing limited partner interests in the Partnership (“common units”) are listed on the New York Stock Exchange (“NYSE”) under the symbol “USAC.” USA Compression GP, LLC, the general partner of the Partnership (the “General Partner”), is owned by USA Compression Holdings, LLC (“USA Compression Holdings”). Unless the context requires otherwise, references to “we,” “us,” “our,” or the “Partnership” are intended to mean the business and operations of the Partnership and its wholly owned, consolidated subsidiaries (the “Operating Subsidiaries”).

The Partnership, through its Operating Subsidiaries, provides compression services under term contracts with customers in the natural gas and crude oil industry, using natural gas compression packages that it designs, engineers, owns, operates and maintains. The unaudited condensed consolidated financial statements include the accounts of the Partnership and the Operating Subsidiaries, and all intercompany balances and transactions have been eliminated in consolidation.

The Partnership’s ownership is as follows:

	June 30, 2016			
	USA Compression Holdings			
		Public	Total	
General partner interest	1.40	%	—	1.40 %
Limited partner interest	41.92	%	56.68 %	98.60 %
Total	43.32	%	56.68 %	100.00 %

Partnership net income is allocated to the partners, both general and limited, in proportion to their respective interest in the Partnership.

(b) Basis of Presentation

The accompanying unaudited condensed consolidated financial statements of the Partnership have been prepared on the same basis as the audited consolidated financial statements included in the Partnership's annual report on Form 10-K for the year ended December 31, 2015 filed on February 11, 2016 (our "2015 Annual Report"). In the opinion of the Partnership's management, such financial information reflects all adjustments necessary for a fair presentation of the financial position as of June 30, 2016 and December 31, 2015, and the results of operations for the three and six months ended June 30, 2016 and 2015, changes in partners' capital for the six months ended June 30, 2016 and the statements of cash flows for the six months ended June 30, 2016 and 2015 in accordance with U.S. generally accepted accounting principles ("GAAP"). Operating results for the three and six months ended June 30, 2016 are not necessarily indicative of the results that may be expected for the year ending December 31, 2016. Certain information and footnote disclosures normally included in annual consolidated financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to the rules and regulations of the U.S. Securities and Exchange Commission (the "SEC"). Therefore, these consolidated financial statements should be read in conjunction with the Partnership's audited consolidated financial statements for the year ended December 31, 2015 contained in our 2015 Annual Report.

(c) Use of Estimates

The unaudited condensed consolidated financial statements of the Partnership have been prepared in conformity with GAAP, which includes the use of estimates and assumptions by management that affect the reported amounts of assets, liabilities, revenues, expenses and disclosure of contingent assets and liabilities that exist at the date of the unaudited condensed consolidated financial statements. Although these estimates are based on management's available knowledge of current and expected future events, actual results could differ from these estimates.

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## (d) Inventories

Inventory consists of serialized and non-serialized parts used primarily in the repair of compression units. Serialized parts inventory is valued at the lower of cost or market value using the specific identification method, while non-serialized parts inventory is valued using the weighted average cost method. Purchases of these assets are considered operating activities in the Unaudited Condensed Consolidated Statement of Cash Flows.

Significant components of inventories as of June 30, 2016 and December 31, 2015 are as follows (in thousands):

	June 30, 2016	December 31, 2015
Serialized parts	\$ 18,653	\$ 18,361
Non-serialized parts	2,343	825
Total Inventory, gross	20,996	19,186
Less: obsolete and slow moving reserve	(314)	(314)
Total Inventory, net	\$ 20,682	\$ 18,872

## (e) Identifiable Intangible Assets

As of June 30, 2016, identifiable intangible assets, net consisted of the following (in thousands):

	Customer Relationships	Trade Names	Non-compete Agreement	Total
Net Balance at December 31, 2015	\$ 65,918	\$ 12,480	\$ 375	\$ 78,773
Amortization Expense	(1,367)	(312)	(113)	(1,792)
Net Balance at June 30, 2016	\$ 64,551	\$ 12,168	\$ 262	\$ 76,981

Identifiable intangible assets are amortized using the straight-line method over their estimated useful lives, which is the period over which the assets are expected to contribute directly or indirectly to the Partnership's future cash flows. The estimated useful lives range from 4 to 30 years. Accumulated amortization of intangible assets was \$18.2 million and \$16.4 million as of June 30, 2016 and December 31, 2015, respectively.

The Partnership assesses identifiable intangible assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. The Partnership did not record any impairment of identifiable intangible assets for the three and six months ended June 30, 2016 or for the three and six months ended June 30, 2015.

(f) Property and Equipment

Property and equipment are carried at cost. Overhauls and major improvements that increase the value or extend the life of compression equipment are capitalized and depreciated over 3 to 5 years. Ordinary maintenance and repairs are charged to cost of operations, exclusive of depreciation and amortization. Depreciation is calculated using the straight-line method over the estimated useful lives of the assets as follows:

Compression equipment, acquired new	25 years
Compression equipment, acquired used	9 - 25 years
Furniture and fixtures	7 years
Vehicles and computer equipment	3 - 7 years
Leasehold improvements	5 years

See more information on property and equipment in Note 3 to our unaudited condensed consolidated financial statements.

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(g) Impairments of Long-Lived Assets

Long-lived assets with recorded values that are not expected to be recovered through future cash flows are written-down to estimated fair value. An asset shall be tested for impairment when events or circumstances indicate that its carrying value may not be recoverable or will no longer be utilized in the operating fleet. The most common circumstance requiring compression units to be tested for impairment is when idle units do not meet the performance characteristics of the Partnership's active revenue generating horsepower. The carrying value of a long-lived asset is not recoverable if it exceeds the sum of the undiscounted cash flows expected to result from the use and eventual disposition of the asset. If the carrying value exceeds the sum of the undiscounted cash flows associated with the operating fleet, an impairment loss equal to the amount of the carrying value exceeding the fair value of the asset is recognized. The fair value of the asset is measured using quoted market prices or, in the absence of quoted market prices, is based on an estimate of discounted cash flows, the expected net sale proceeds compared to the other similarly configured fleet assets the Partnership recently sold or a review of other assets recently offered for sale by third parties, or the estimated component value of the equipment the Partnership plans to use.

During the three and six months ended June 30, 2016, the Partnership evaluated the future deployment of its idle fleet under current market conditions and determined to retire and either sell or re-utilize the key components of 5 compression units, with a total of approximately 1,700 horsepower, that were previously used to provide services in the Partnership's business. During the three and six months ended June 30, 2015, the Partnership evaluated the future deployment of its idle fleet under current market conditions and determined to retire and either sell or re-utilize the key components of 166 compression units, with a total of approximately 58,000 horsepower, that were previously used to provide services in the Partnership's business. In both periods, the cause of the impairment was related to certain performance characteristics of the impaired equipment, such as excessive maintenance costs and the inability of the equipment to meet current emission standards without retrofitting. We determined that this equipment was unlikely to be accepted by customers under current market conditions. This compression equipment was written down to its respective estimated salvage value, measured using quoted market prices, or the estimated component value of the equipment the Partnership plans to use. As a result of the Partnership's decision to retire, sell or re-utilize these compressor units, management performed an impairment review and based on that review, recorded a \$0.7 million impairment of long-lived assets in the three and six months ended June 30, 2016. The Partnership recorded a \$26.8 million impairment of long-lived assets in the three and six months ended June 30, 2015.

(h) Fair Value Measurements

Accounting standards on fair value measurements establish a framework for measuring fair value and stipulate disclosures about fair value measurements. The standards apply to recurring and nonrecurring financial and non-financial assets and liabilities that require or permit fair value measurements. Among the required disclosures is the fair value hierarchy of inputs the Partnership uses to value an asset or a liability. The three levels of the fair value hierarchy are described as follows:



Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the Partnership has the ability to access at the measurement date.

Level 2 inputs are those other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.

Level 3 inputs are unobservable inputs for the asset or liability.

As of June 30, 2016 and 2015, the Partnership's financial instruments consisted primarily of cash and cash equivalents, trade accounts receivable, trade accounts payable and long-term debt. The book values of cash and cash equivalents, trade accounts receivable and trade accounts payable are representative of fair value due to their short-term maturity. The carrying amount of long-term debt approximates fair value due to the floating interest rates associated with the debt.

Phantom unit awards granted to employees under the USA Compression Partners, LP 2013 Long-Term Incentive Plan (the "LTIP") are accounted for as a liability, and such liability is re-measured on a quarterly basis. The liability is based on the publicly quoted price of the Partnership's common units, which is considered a Level 1 input. As of

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June 30, 2016 and December 31, 2015, the total unit-based compensation liability was \$3.2 million and \$2.0 million, respectively.

(i) Operating Segment

The Partnership operates in a single business segment, the compression services business.

(j) Pass Through Taxes

Sales taxes incurred on behalf of, and passed through to, customers are accounted for on a net basis.

(2) Trade Accounts Receivable

Trade accounts receivable are recorded at the invoiced amount and do not bear interest. The allowance for doubtful accounts, which was \$0.7 million and \$2.1 million at June 30, 2016 and December 31, 2015, respectively, is the Partnership's best estimate of the amount of probable credit losses included in the Partnership's existing accounts receivable. The Partnership determines the allowance based upon historical write-off experience and specific customer circumstances. The determination of the allowance for doubtful accounts requires us to make estimates and judgments regarding our customers' ability to pay amounts due. On an ongoing basis, we conduct an evaluation of the financial strength of our customers based on payment history, the overall business climate in which our customers operate and specific identification of customer bad debt and make adjustments to the allowance as necessary. Our evaluation of our customers' financial strength is based on the aging of their respective receivables balance, customer correspondence, financial information and third-party credit ratings. Our evaluation of the business climate in which our customers operate is based on a review of various publicly-available materials regarding our customers' industries, including the solvency of various companies in the industry. The aforementioned factors reviewed by the Partnership led to an increase in the allowance account during the twelve months ended December 31, 2015. During the three and six months ended June 30, 2016, the Partnership decreased its allowance for doubtful accounts by \$0.6 million and \$1.4 million, respectively. This was due in part to collections on accounts that had previously been reserved due to bankruptcy or significantly delinquent balances. Also contributing to the decrease in the allowance for doubtful accounts during the three months ended June 30, 2016 was the write-off of \$0.2 million of accounts that had been previously reserved. The Partnership does not have any off-balance-sheet credit exposure related to its customers. Since the overall energy industry continues to be volatile, it is not certain that the factors leading to an increase in the allowance for doubtful accounts during 2015, or the subsequent decrease during 2016, will continue.

(3) Property and Equipment

Property and equipment consisted of the following as of June 30, 2016 and December 31, 2015 (in thousands):

	June 30, 2016	December 31, 2015
Compression equipment	\$ 1,545,046	\$ 1,520,835
Furniture and fixtures	625	669
Automobiles and vehicles	18,981	19,284
Computer equipment	22,508	21,457
Leasehold improvements	1,267	1,197
Total	1,588,427	1,563,442
Less accumulated depreciation and amortization	(287,866)	(245,399)
Total	\$ 1,300,561	\$ 1,318,043

We recognized \$22.5 million and \$20.6 million of depreciation expense on property and equipment for the three months ended June 30, 2016 and 2015, respectively. We recognized \$43.7 million and \$40.4 million of depreciation expense on property and equipment for the six months ended June 30, 2016 and 2015, respectively.

As of June 30, 2016 and December 31, 2015, there was \$16.7 million and \$13.1 million, respectively, of property and equipment purchases in accounts payable and accrued liabilities.

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During the three and six months ended June 30, 2015, insurance recoveries of \$0.2 million were received on previously impaired compression equipment. During the three and six months ended June 30, 2016, we transferred property and equipment and incurred a \$1.0 million loss associated with the portion of the property and equipment that was not transferable. Each of these are reported within the Loss (gain) on sale of assets line in the Unaudited Condensed Consolidated Statements of Operations.

(4) Installment Receivable

On June 30, 2014, the Partnership entered into a FMV Bargain Purchase Option Grant Agreement (the “Capital Lease Transaction”) with a customer, pursuant to which the Partnership granted a bargain purchase option to the customer with respect to certain compressor packages leased to the customer (each a “Subject Compressor Package”). The bargain purchase option provides the customer with an option to acquire the equipment at a value significantly less than the fair market value at the end of the lease term.

The Capital Lease Transaction was accounted for as a sales type lease and resulted in a current installment receivable of \$3.1 million and \$3.0 million as of June 30, 2016 and December 31, 2015, respectively, included in Other accounts receivable, and a long-term installment receivable of \$15.7 million and \$17.3 million, respectively.

Revenue and interest income related to the Capital Lease Transaction is recognized over the lease term which is 7 years. The Partnership recognizes maintenance revenue within Contract operations revenue and interest income within Interest expense, net on the Statements of Operations. For each of the three months ended June 30, 2016 and 2015, maintenance revenue related to the Capital Lease Transaction was \$0.3 million. For each of the six months ended June 30, 2016 and 2015, maintenance revenue related to the Capital Lease Transaction was \$0.6 million. Interest income was \$0.4 million in each of the three months ended June 30, 2016 and 2015 and \$0.7 million and \$0.8 million in the six months ended June 30, 2016 and 2015, respectively.

(5) Accrued Liabilities

Other current liabilities included accrued payroll and benefits and accrued property taxes. The Partnership recognized \$5.7 million and \$7.1 million of accrued payroll and benefits as of June 30, 2016 and December 31, 2015, respectively. The Partnership recognized \$6.0 million and \$4.1 million of accrued property taxes as of June 30, 2016 and December 31, 2015, respectively.

(6) Income Tax Expense

The Partnership is not a taxable entity for U.S. federal income tax purposes or for the majority of states that impose an income tax. Therefore, income taxes are not levied at the entity level, but rather on the individual partners of the Partnership. Accordingly, the accompanying unaudited condensed consolidated financial statements do not include a provision for federal and state income taxes.

The Partnership is subject to the Revised Texas Franchise Tax (“Texas Margin Tax”). The Texas Margin Tax is computed on modified gross margin. The Partnership does not do business in any other state where a similar tax is applied.

Components of income tax expense are as follows (in thousands):

	Three months ended June 30,		Six months ended June 30,	
	2016	2015	2016	2015
Current tax expense:				
State income tax	\$ 62	\$ 142	\$ 194	\$ 221
Total current tax expense	62	142	194	221
Deferred tax expense:				
State income tax	\$ 32	\$ —	\$ 134	\$ —
Total deferred tax expense	32	—	134	—
Total income tax expense	\$ 94	\$ 142	\$ 328	\$ 221

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Deferred income tax balances are the direct effect of temporary differences between the financial statement carrying amounts and the tax basis of assets and liabilities at the enacted tax rates expected to be in effect when the taxes are actually paid or recovered. The tax effects of temporary differences that give rise to deferred tax liabilities are as follows (in thousands):

	June 30, 2016	December 31, 2015
Deferred tax liabilities		
Property and equipment	\$ 1,008	\$ 874
Total deferred tax liabilities	1,008	874
Net deferred tax liabilities	\$ 1,008	\$ 874

The Financial Accounting Standards Board's ("FASB") Accounting Standards Codification Topic 740-10 ("ASC 740-10") provides guidance on measurement and recognition in accounting for income tax uncertainties and provides related guidance on derecognition, classification, disclosure, interest, and penalties. As of June 30, 2016, the Partnership had no material unrecognized tax benefits (as defined in ASC 740-10). The Partnership does not expect to incur interest charges or penalties related to our tax positions, but if such charges or penalties are incurred, the Partnership's policy is to account for interest charges as Interest expense, net and penalties as Income tax expense in the Unaudited Condensed Consolidated Statements of Operations.

## (7) Long-Term Debt

The long-term debt of the Partnership, of which there is no current portion, consisted of the following as of June 30, 2016 and December 31, 2015 (in thousands):

	June 30, 2016	December 31, 2015
Revolving Credit Facility	\$ 735,120	\$ 729,187

## Revolving Credit Facility

In March 2016, the Partnership entered into a third amendment to its revolving credit facility, which amended the credit agreement to, among other things, (i) modify the leverage ratio covenant to be (A) 5.95 to 1.0 as of the end of the respective fiscal quarters ending June 30, 2016 and September 30, 2016, (B) 5.75 to 1.0 as of the end of the fiscal quarter ending December 31, 2016, (C) 5.50 to 1.0 as of the end of the respective fiscal quarters ending March 31,

2017 and June 30, 2017, (D) 5.25 to 1.0 as of the end of the respective fiscal quarters ending September 30, 2017 and December 31, 2017 and (E) 5.00 to 1.0 thereafter, and (ii) amend certain other provisions of the credit agreement, all as more fully set forth in the third amendment.

In connection with entering into the third amendment, the Partnership paid certain amendment fees to the lenders party thereto and paid a certain arrangement fee to the arranger of the third amendment in the amount of \$2.0 million, collectively, during the six months ended June 30, 2016. The Partnership paid \$3.4 million in various loan fees and costs incurred related to the second amendment to our revolving credit facility during the six months ended June 30, 2015. An immaterial amount of such fees were paid during the three months ended June 30, 2016 and no such fees were paid during the three months ended June 30, 2015. These fees were capitalized to loan costs and will be amortized through January 2020.

As of June 30, 2016, the Partnership was in compliance with all of its covenants under its revolving credit facility.

As of June 30, 2016, the Partnership had outstanding borrowings under its revolving credit facility of \$735.1 million, \$364.9 million of borrowing base availability and, subject to compliance with the applicable financial covenants, available borrowing capacity of \$146.0 million. The Partnership's interest rate in effect for all borrowings under its revolving credit facility as of June 30, 2016 and December 31, 2015 was 2.51% and 2.26%, respectively, with a weighted average interest rate of 2.47% and 2.19% during the three months ended June 30, 2016 and 2015, respectively, and 2.47% and 2.19% during the six months ended June 30, 2016 and 2015, respectively. There were no letters of credit issued as of June 30, 2016 or 2015.

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In the event that any of the Operating Subsidiaries guarantees any series of the debt securities as described in the Partnership's registration statement filed on Form S-3 (Reg. No. 333-193724), such guarantees will be full and unconditional and made on a joint and several basis for the benefit of each holder and the Trustee. However, such guarantees will be subject to release, subject to certain limitations, as follows (i) upon the sale, exchange or transfer, whether by way of a merger or otherwise, to any Person that is not an Affiliate of the Partnership, of all the Partnership's direct or indirect limited partnership or other equity interest in such Subsidiary Guarantor; or (ii) upon the Partnership's or USA Compression Finance Corp.'s (together, the "Issuers") delivery of a written notice to the Trustee of the release or discharge of all guarantees by such Subsidiary Guarantor of any Debt of the Issuers other than obligations arising under the indenture governing such debt and any debt securities issued under such indenture, except a discharge or release by or as a result of payment under such guarantees. Capitalized terms used but not defined in this paragraph are defined in the Form of Indenture filed as exhibit 4.1 to such registration statement.

The revolving credit facility matures in January 2020 and the Partnership expects to maintain this facility for the term.

### (8) Partners' Capital

#### Common Units and General Partner Interest

As of June 30, 2016, the Partnership had 54,866,123 common units outstanding. USA Compression Holdings held 23,328,315 common units as of June 30, 2016 and controlled the General Partner which held an approximate 1.40% general partner interest (the "General Partner's Interest") and the incentive distribution rights ("IDRs"). The number of common units outstanding on this date includes 14,048,588 common units issued through the conversion of subordinated units on a one-for-one basis on February 16, 2016. See the Unaudited Condensed Consolidated Statement of Changes in Partners' Capital.

#### Subordinated Units

Upon the payment of the February 12, 2016 cash distribution, the Partnership satisfied the requirements contained in the Partnership's limited partnership agreement for the automatic conversion of all outstanding subordinated units into common units on a one-for-one basis. As a result, on February 16, 2016, all of the outstanding subordinated units converted to common units on a one-for-one basis. The conversion of subordinated units does not impact the amount of cash distributions we pay or the total number of our outstanding units.

#### Cash Distributions



The Partnership has declared quarterly distributions per unit to limited partner unitholders of record, including holders of common, subordinated units and phantom units and distributions paid to the General Partner, including the General Partner's Interest and IDRs, as follows (dollars in millions, except distribution per unit):

Payment Date	Distribution per Limited Partner Unit	Amount Paid to Common Unitholders	Amount Paid to Subordinated Unitholder	Amount Paid to General Partner	Amount Paid to Phantom Unitholders	Amount Paid to Total Distribution
May 15, 2015	0.515	16.6	7.2	0.6	0.2	24.6
August 14, 2015	0.525	17.2	7.4	0.7	0.2	25.5
November 13, 2015	0.525	19.7	7.4	0.7	0.2	28.0
February 12, 2016	0.525	20.2	7.4	0.7	0.8	29.1
May 13, 2016	0.525	28.4	—	0.7	0.7	29.8

#### Announced Quarterly Distribution

On July 21, 2016, the Partnership announced a cash distribution of \$0.525 per unit on its common units. The distribution will be paid on August 12, 2016 to unitholders of record as of the close of business on August 2, 2016. USA Compression Holdings, the owner of approximately 42.5% of the Partnership's outstanding limited partner interests, has elected to reinvest 50% of this distribution with respect to its units pursuant to the Partnership's distribution reinvestment plan (the "DRIP").

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### Dividend Reinvestment Program

During the six months ended June 30, 2016 and 2015, distributions of \$21.3 million and \$27.0 million, respectively, were reinvested under the DRIP resulting in the issuance of 2.1 million and 1.3 million common units, respectively. Such distributions are treated as non-cash transactions in the accompanying Unaudited Condensed Consolidated Statements of Cash Flows.

### Earnings Per Common and Subordinated Unit

The computations of earnings per common unit and subordinated unit are based on the weighted average number of common units and subordinated units, respectively, outstanding during the applicable period. The subordinated units and the General Partner's Interest (including its IDRs) meet the definition of participating securities as defined by the FASB's Accounting Standards Codification Topic 260 Earnings Per Share; therefore, the Partnership is required to use the two-class method in the computation of earnings per unit. Basic earnings per common and subordinated unit are determined by dividing net income allocated to the common and subordinated units, respectively, after deducting the amount allocated to the General Partner (including distributions to the General Partner on the General Partner's Interest and its IDRs), by the weighted average number of outstanding common and subordinated units, respectively, during the period. Net income is allocated to the common units, subordinated units and the General Partner's Interest (including its IDRs) based on their respective shares of the distributed and undistributed earnings for the period. To the extent cash distributions exceed net income for the period, the excess distributions are allocated to all participating units outstanding based on their respective ownership percentages. Diluted earnings per unit are computed using the treasury stock method, which considers the potential issuance of limited partner units associated with the LTIP. Unvested phantom units are not included in basic earnings per unit, as they are not considered to be participating securities, but are included in the calculation of diluted earnings per unit. For the three and six months ended June 30, 2015, approximately 74,000 and 106,000 incremental phantom units, respectively, were excluded from the calculation of diluted units because the impact was anti-dilutive.

Due to the conversion of subordinated units to common units in February 2016, the subordinated units did not participate in any of the distributed earnings for the six month period, resulting in a negative earnings per unit value for the six months ended June 30, 2016.

### Incentive Distribution Rights

The General Partner holds all of the IDRs. The following table illustrates the percentage allocations of Available Cash from Operating Surplus between the unitholders and the General Partner based on the specified target distribution levels. The amounts set forth under "Marginal Percentage Interest in Distributions" are the percentage interests of the General Partner and the unitholders in any Available Cash from Operating Surplus the Partnership distributes up to

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and including the corresponding amount in the column “Total Quarterly Distribution Per Unit.” The percentage interests shown for the Partnership’s unitholders and the General Partner for the minimum quarterly distribution are also applicable to quarterly distribution amounts that are less than the minimum quarterly distribution. The percentage interests set forth below for the General Partner include its General Partner’s Interest, and assume the General Partner has contributed any additional capital necessary to maintain its General Partner’s Interest, the General Partner has not transferred the IDRs and there are no arrearages on common units.

	Total Quarterly Distribution Per Unit	Marginal Percentage Interest in Distributions	
		Unitholder	General Partner
Minimum Quarterly Distribution	\$0.425	98.60%	1.40%
First Target Distribution	up to \$0.4888	98.60%	1.40%
Second Target Distribution	above \$0.4888 up to \$0.5313	85.60%	14.40%
Third Target Distribution	above \$0.5313 up to \$0.6375	75.60%	24.40%
Thereafter	above \$0.6375	50.60%	49.40%

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(9) Transactions with Related Parties

John Chandler, who has served as a director of the General Partner since October 2013, has served as a director of a customer since October 2014. During the three months ended June 30, 2016 and 2015, the Partnership recognized \$2.2 million and \$2.2 million, respectively, and \$4.4 million and \$4.0 million during the six months ended June 30, 2016 and 2015, respectively, in revenue on compression services and \$1.1 million and \$1.3 million in accounts receivable from this customer on the Unaudited Condensed Consolidated Statements of Operations for the three and six months ended June 30, 2016 and 2015 and the Unaudited Condensed Consolidated Balance Sheet as of June 30, 2016 and December 31, 2015, respectively.

(10) Commitments and Contingencies

(a) Major Customers

The Partnership did not have revenue from any single customer representing greater than 10% of total revenue for the three or six months ended June 30, 2016. The Partnership had revenue from one customer representing 10.3% and 10.5% of total revenue for the three and six months ended June 30, 2015, respectively. No other customer represented greater than 10% of total revenue for the three and six months ended June 30, 2015.

(b) Litigation

From time to time, the Partnership and its subsidiaries may be involved in various claims and litigation arising in the ordinary course of business. In management's opinion, the resolution of such matters is not expected to have a material adverse effect on the Partnership's consolidated financial position, results of operations or cash flows.

(c) Equipment Purchase Commitments

The Partnership's future capital commitments are comprised of binding commitments under purchase orders for new compression units and serialized parts ordered but not received. The commitments as of June 30, 2016 were \$7.2 million, all of which are expected to be settled within the next twelve months.

(d) Sales Tax Contingency

The Partnership is subject to a number of state and local taxes that are not income-based. As many of these taxes are subject to audit by the taxing authorities, it is possible that an audit could result in additional taxes due. We accrue for such additional taxes when we determine that it is probable that we have incurred a liability and we can reasonably estimate the amount of the liability. As of June 30, 2016, we have accrued a liability of \$0.2 million for additional taxes. We believe that it is reasonably possible that we could incur losses beyond what has been accrued. Due to uncertainty related to the documentation required by certain state auditors, we are unable at this time to project a reasonable range of the extent of losses we may incur beyond what we have accrued.

(11) Recent Accounting Pronouncement

In July 2015, the FASB agreed to defer by one year the mandatory effective date of its revenue recognition standard to annual and interim periods in fiscal years beginning after December 15, 2017, but will also provide entities the option to adopt it as of the original effective date. The option to use either a retrospective or cumulative-effect transition method will not change. The Partnership is currently evaluating the impact, if any, of this Accounting Standards Update (“ASU”) on its consolidated financial statements.

Also in July 2015, the FASB issued an ASU that changes the measurement principle for inventory from the lower of cost or market to the lower of cost and net realizable value. This ASU requires prospective adoption for inventory measurements for annual and interim periods in fiscal years beginning after December 15, 2016. Early adoption is permitted. The Partnership is currently evaluating the impact, if any, of this ASU on its consolidated financial statements.

In February 2016, the FASB issued a new leasing standard that increases transparency and comparability among organizations by, among other things, requiring lessees to recognize lease assets and lease liabilities on the balance sheet

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and requiring both lessees/lessors to disclose expanded qualitative and quantitative information about leasing arrangements. Lessor accounting will remain substantially similar to current U.S. GAAP but with some changes to conform and align guidance with the new lessee guidance and other areas within U.S. GAAP, such as Accounting Standards Codification Topic 606, Revenue from Contracts with Customers. This ASU requires modified retrospective adoption, with elective reliefs, and becomes effective for public business entities for annual and interim periods in fiscal years beginning after December 15, 2018. The Partnership is currently evaluating the impact, if any, of this ASU on its consolidated financial statements.

In March 2016, the FASB issued an ASU that clarifies the implementation guidance on principal versus agent considerations. The amendments are intended to improve the operability and understandability of the implementation guidance on principal versus agent considerations within the revenue recognition update. The effective date and transition requirements for the amendments in this update are the same as the effective date and transition requirements of the revenue recognition update. The Partnership is currently evaluating the impact, if any, of this ASU along with the revenue recognition ASU, on its consolidated financial statements.

In March 2016, the FASB issued an ASU that simplifies several aspects of accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. For public business entities, the amendments within this ASU are effective for annual and interim periods in fiscal years beginning after December 15, 2016. Early adoption is permitted. The Partnership is currently evaluating the impact, if any, of this ASU on its consolidated financial statements.

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ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

DISCLOSURE REGARDING FORWARD-LOOKING STATEMENTS

This report contains "forward-looking statements." All statements other than statements of historical fact contained in this report are forward-looking statements, including, without limitation, statements regarding our plans, strategies, prospects and expectations concerning our business, results of operations and financial condition. You can identify many of these statements by looking for words such as "believe," "expect," "intend," "project," "anticipate," "estimate," "contingent" or similar words or the negative thereof.

Known material factors that could cause our actual results to differ from those in these forward-looking statements are described in Part II, Item 1A ("Risk Factors") and elsewhere in this report. Important factors that could cause our actual results to differ materially from the expectations reflected in these forward-looking statements include, among other things:

- changes in general economic conditions and changes in economic conditions of the crude oil and natural gas industry specifically;
- competitive conditions in our industry;
- changes in the long-term supply of and demand for crude oil and natural gas;
- our ability to realize the anticipated benefits of acquisitions and to integrate the acquired assets with our existing fleet;
  - actions taken by our customers, competitors and third-party operators;
- the deterioration of the financial condition of our customers;
- changes in the availability and cost of capital;
- operating hazards, natural disasters, weather-related delays, casualty losses and other matters beyond our control;

- the effects of existing and future laws and governmental regulations; and
- the effects of future litigation.

All forward-looking statements included in this report are based on information available to us on the date of this report and speak only as of the date of this report. Except as required by law, we undertake no obligation to publicly update or revise any forward-looking statement, whether as a result of new information, future events or otherwise. All subsequent written and oral forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by the foregoing cautionary statements.

## Overview

We provide compression services in a number of shale plays throughout the U.S., including the Utica, Marcellus, Permian Basin, Delaware Basin, Eagle Ford, Mississippi Lime, Granite Wash, Woodford, Barnett, Haynesville, Niobrara and Fayetteville shales. The demand for our services is driven by the domestic production of natural gas and crude oil; as such, we have focused our activities in areas with attractive natural gas and crude oil production growth, which are generally found in these shale and unconventional resource plays. While our business focuses largely on compression services serving infrastructure installations, including centralized natural gas gathering systems and processing facilities, which utilize large horsepower compression units, typically in shale plays, we also provide compression services in more mature conventional basins, including gas lift applications on crude oil wells employing horizontal drilling techniques. Gas lift and other artificial lift technologies are critical to the enhancement of production of oil from horizontal wells operating in tight shale plays.



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## Operating Highlights

The following table summarizes certain horsepower and horsepower utilization percentages for the periods presented.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Fleet horsepower (at period end) (1)	1,718,757	1,631,959	1,718,757	1,631,959
Total available horsepower (at period end) (2)	1,728,237	1,639,064	1,728,237	1,639,064
Revenue generating horsepower (at period end) (3)	1,359,523	1,411,005	1,359,523	1,411,005
Average revenue generating horsepower (4)	1,378,496	1,405,039	1,394,535	1,395,473
Average revenue per revenue generating horsepower per month (5)	\$ 15.52	\$ 15.83	\$ 15.62	\$ 15.84
Revenue generating compression units (at period end)	2,558	2,733	2,558	2,733
Average horsepower per revenue generating compression unit (6)	530	518	528	518
Horsepower utilization (7):				
At period end	86.0	% 91.5	% 86.0	% 91.5
Average for the period (8)	86.1	% 90.5	% 87.4	% 91.2

(1) Fleet horsepower is horsepower for compression units that have been delivered to us (and excludes units on order). As of August 2, 2016, we had 7,110 horsepower on order for delivery in the remainder of 2016.

(2) Total available horsepower is revenue generating horsepower under contract for which we are billing a customer, horsepower in our fleet that is under contract but is not yet generating revenue, horsepower not yet in our fleet that is under contract but not yet generating revenue and that is subject to a purchase order, and idle horsepower. Total available horsepower excludes new horsepower on order for which we do not have a compression services contract.

(3) Revenue generating horsepower is horsepower under contract for which we are billing a customer.

(4) Calculated as the average of the month-end revenue generating horsepower for each of the months in the period.

(5) Calculated as the average of the result of dividing the contractual monthly rate for all units at the end of each month in the period by the sum of the revenue generating horsepower at the end of each month in the period.

- (6) Calculated as the average of the month-end revenue generating horsepower per revenue generating compression unit for each of the months in the period.
- (7) Horsepower utilization is calculated as (i) the sum of (a) revenue generating horsepower, (b) horsepower in our fleet that is under contract but is not yet generating revenue, and (c) horsepower not yet in our fleet that is under contract, not yet generating revenue and is subject to a purchase order, divided by (ii) total available horsepower less idle horsepower that is under repair. Horsepower utilization based on revenue generating horsepower and fleet horsepower as of June 30, 2016 and 2015 was 79.1% and 86.5%, respectively.
- (8) Calculated as the average utilization for the months in the period based on utilization at the end of each month in the period. Average horsepower utilization based on revenue generating horsepower and fleet horsepower for the three months ended June 30, 2016 and 2015 was 80.4% and 84.9%, respectively. Average horsepower utilization based on revenue generating horsepower and fleet horsepower for the six months ended June 30, 2016 and 2015 was 81.4% and 85.8%, respectively.

The 5.3% increase in fleet horsepower as of June 30, 2016 over the fleet horsepower as of June 30, 2015 was attributable to the compression units added to our fleet to meet the then expected incremental demand by new and current customers for our compression services. The 1.9% decrease in average revenue generating horsepower for the three months ended June 30, 2016 over June 30, 2015 was primarily attributable to an increase in the amount of time contracting new compression units and an increase in the amount of compression units returned to us. The 2.0% and 1.4% decrease in average revenue per revenue generating horsepower per month for the three and six months ended June 30, 2016 over June 30, 2015, respectively, was primarily due to reduced pricing in the small horsepower portion of our fleet over the three and six months ended June 30, 2016 as compared to pricing for those units over the three and six months ended June 30, 2015.

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Average horsepower utilization decreased approximately 4.4% during the three months ended June 30, 2016 compared to the three months ended June 30, 2015. The decrease in average horsepower utilization is primarily attributable to the following changes as a percentage of total available horsepower: (1) a 4% increase in our average fleet of compression units returned to us not yet under contract and (2) a 2.8% decrease in horsepower that is on-contract or pending-contract but not yet active. The decrease in average horsepower utilization was offset by a 3.0% increase in idle horsepower under repair, as a percentage of total available horsepower, which is excluded from the average horsepower utilization calculation until such repair is complete. We believe the decrease in average horsepower utilization is the result of a delay in planned projects of certain of our customers, continued optimization of existing compression service requirements and our selective pursuit of what we deem to be the most attractive opportunities. The above described fluctuation in utilization components explains the changes in both period end and average horsepower utilization between the six months ended June 30, 2016 and the six months ended June 30, 2015.

Average horsepower utilization based on revenue generating horsepower and fleet horsepower decreased approximately 4.5% during the three months ended June 30, 2016 compared to the three months ended June 30, 2015. The decrease is primarily attributable to the following changes as a percentage of total fleet horsepower: (1) a 3.5% increase in our average idle fleet from compression units returned to us and (2) a 3.0% increase in idle horsepower under repair offset by (3) a 2.0% decrease in our average idle fleet composed of new compression units. The increase in units returned to us is believed to be a result of our customers' optimization of their compression service requirements. The above described fluctuation in utilization components explains the changes in both period end and average horsepower utilization based on revenue generating horsepower and fleet horsepower between the six months ended June 30, 2016 and the six months ended June 30, 2015.

## Financial Results of Operations

Three months ended June 30, 2016 compared to the three months ended June 30, 2015

The following table summarizes our results of operations for the periods presented (dollars in thousands):

	Three Months Ended June 30, 2016	Three Months Ended June 30, 2015	Percent Change	
Revenues:				
Contract operations	\$ 62,785	\$ 65,552	(4.2)	%
Parts and service	726	838	(13.4)	%
Total revenues	63,511	66,390	(4.3)	%
Costs and expenses:				
Cost of operations, exclusive of depreciation and amortization	18,654	19,079	(2.2)	%

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Gross Operating Margin	44,857	47,311	(5.2)	%
Other operating and administrative costs and expenses:				
Selling, general and administrative	11,180	10,350	8.0	%
Depreciation and amortization	23,412	21,507	8.9	%
Loss (gain) on sale of assets	1,072	(23)	(4,760.9)	%
Impairment of compression equipment	693	26,829	(97.4)	%
Total other operating and administrative costs and expenses	36,357	58,663	(38.0)	%
Operating income (loss)	8,500	(11,352)	(174.9)	%
Other income (expense):				
Interest expense, net	(5,139)	(4,415)	16.4	%
Other	7	5	40.0	%
Total other expense	(5,132)	(4,410)	16.4	%
Income before income tax expense	3,368	(15,762)	(121.4)	%
Income tax expense	94	142	(33.8)	%
Net income (loss)	\$ 3,274	\$ (15,904)	(120.6)	%

Contract operations revenue. During the three months ended June 30, 2016, we experienced a year-to-year decrease in demand for our compression services driven by decreased operating activity in natural gas and crude oil production and continued optimization of existing compression service requirements, resulting in a 1.9% decrease in average

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revenue generating horsepower and a \$2.8 million decrease in our contract operations revenue. Average revenue per revenue generating horsepower per month decreased from \$15.83 for the three months ended June 30, 2015 to \$15.52 for the three months ended June 30, 2016, a decrease of 2.0%, attributable, in part, to reduced pricing in the small horsepower portion of our fleet, offset by slightly improved pricing in the large horsepower portion of our fleet. Average revenue per revenue generating horsepower per month associated with our compression services provided on a month-to-month basis did not significantly differ from the average revenue per revenue generating horsepower per month associated with our compression services provided under contracts in the primary term.

Because the demand for our services is driven primarily by production of natural gas, we focus our activities in areas of attractive growth, which are generally found in certain shale and unconventional resource plays. Our contract operations revenue was not materially impacted by any renegotiations of our contracts during the period with our customers.

Parts and service revenue. Parts and service revenue was earned on freight and crane charges that are directly reimbursable by our customers, for which we earn little to no margin, and maintenance work and general contract services on customer-owned units and infrastructure, for which we earn lower margins than our contract operations. We offered these services as a courtesy to our customers and the demand fluctuates from period to period based on the varying needs of our customers.

Cost of operations, exclusive of depreciation and amortization. The \$0.4 million decrease in cost of operations consisted of a \$0.8 million decrease in direct expenses such as parts and fluids expenses and a \$0.3 million decrease in expenses related to our vehicle fleet, offset by a \$0.6 million increase in indirect expenses, the majority of which were higher property and other taxes.

Gross operating margin. The \$2.5 million decrease in Gross operating margin, or 0.7% decrease in Gross operating margin percentage, was primarily due to a decrease in revenues during the three months ended June 30, 2016, partially offset by a decrease in operating expenses.

Selling, general and administrative expense. The \$0.8 million increase in selling, general and administrative expense for the three months ended June 30, 2016 was primarily attributable to a \$1.8 million increase in unit-based compensation expense, offset by a \$0.8 million decrease in bad debt expense.

Depreciation and amortization expense. The \$1.9 million increase in depreciation and amortization expense was entirely related to an increase in gross property and equipment balances during the three months ended June 30, 2016 compared to gross balances during the three months ended June 30, 2015. There was no variance in amortization expense between the same periods, as intangible assets are amortized on a straight-line basis and there has been no change in gross identifiable intangible assets between the periods.

Loss (gain) on sale of assets. During the three months ended June 30, 2016 we transferred property and equipment and incurred a \$1.0 million loss associated with the portion of the property and equipment that was not transferable.

Impairment on compression equipment. The \$0.7 million and \$26.8 million impairment charge during the three months ended June 30, 2016 and 2015, respectively, resulted from our evaluation of the future deployment of our current idle fleet under the current market conditions. Our evaluation determined that due to certain performance characteristics of the impaired equipment, such as excessive maintenance costs and the inability of the equipment to meet current emission standards without retrofitting, this equipment was unlikely to be accepted by customers under current market conditions. As a result of our evaluation during the three months ended June 30, 2016 and 2015, we determined to retire and either sell or re-utilize the key components of 5 and 166 compression units, respectively, with a total of approximately 1,700 and 58,000 horsepower, respectively, that had been previously used to provide compression services in our business.

Interest expense, net. The \$0.7 million increase in interest expense, net was primarily attributable to the impact of an increase in the weighted average interest rate. Our revolving credit facility bore an interest rate of 2.51% and 2.19% at June 30, 2016 and 2015, respectively, and a weighted average interest rate of 2.47% and 2.19% for the three months ended June 30, 2016 and 2015, respectively. The increase in interest rate was offset by a \$1.5 million decrease in average outstanding borrowings under our revolving credit facility, for which average borrowings were \$739.8 million for the three months ended June 30, 2016 compared to \$741.3 million for the three months ended June 30, 2015.

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Six months ended June 30, 2016 compared to the six months ended June 30, 2015

The following table summarizes our results of operations for the periods presented (dollars in thousands):

	Six Months Ended June 30,		Percent	
	2016	2015	Change	
Revenues:				
Contract operations	\$ 127,063	\$ 129,587	(1.9)	%
Parts and service	2,815	1,803	56.1	%
Total revenues	129,878	131,390	(1.2)	%
Costs and expenses:				
Cost of operations, exclusive of depreciation and amortization	39,483	38,290	3.1	%
Gross Operating Margin	90,395	93,100	(2.9)	%
Other operating and administrative costs and expenses:				
Selling, general and administrative	20,919	20,079	4.2	%
Depreciation and amortization	45,506	42,238	7.7	%
Loss (gain) on sale of assets	950	(218)	(535.8)	%
Impairment of compression equipment	693	26,829	(97.4)	%
Total other operating and administrative costs and expenses	68,068	88,928	(23.5)	%
Operating income	22,327	4,172	435.2	%
Other income (expense):				
Interest expense, net	(10,201)	(8,409)	21.3	%
Other	14	10	40.0	%
Total other expense	(10,187)	(8,399)	21.3	%
Income before income tax expense	12,140	(4,227)	(387.2)	%
Income tax expense	328	221	48.4	%
Net income (loss)	\$ 11,812	\$ (4,448)	(365.6)	%

Contract operations revenue. During the six months ended June 30, 2016, we experienced a year-to-year decrease in demand for our compression services driven by decreased operating activity in natural gas and crude oil production and continued optimization of existing compression service requirements, and a decrease in average revenue per revenue generating horsepower per month resulting in a \$2.5 million decrease in our contract operations revenue. Average revenue per revenue generating horsepower per month decreased from \$15.84 for the six months ended June 30, 2015 to \$15.62 for the six months ended June 30, 2016, a decrease of 1.4%, attributable, in part, to reduced pricing in the small horsepower portion of our fleet, offset by improved pricing in the large horsepower portion of our fleet. Average revenue per revenue generating horsepower per month associated with our compression services provided on a month-to-month basis did not significantly differ from the average revenue per revenue generating horsepower per month associated with our compression services provided under contracts in the primary term. Because the demand for our services is driven primarily by production of natural gas, we focus our activities in areas of attractive growth, which are generally found in certain shale and unconventional resource plays. Our contract operations revenue was not materially impacted by any renegotiations of our contracts during the period with our customers.

Parts and service revenue. Parts and service revenue was earned on freight and crane charges that are directly reimbursable by our customers, for which we earn little to no margin, and maintenance work and general contract services on customer-owned units and infrastructure, for which we earn lower margins than our contract operations. We offered these services as a courtesy to our customers and the demand fluctuates from period to period based on the varying needs of our customers.

Cost of operations, exclusive of depreciation and amortization. The \$1.2 million increase in cost of operations was primarily attributable to a \$1.3 million increase in indirect expenses, the majority of which were higher property and other taxes, a \$0.8 million increase in retail parts and service expenses, which have a corresponding increase in parts and service revenue, and a \$0.7 million increase in direct labor expenses associated with our contract operations, offset by a \$1.2 million decrease in direct expenses such as parts and fluids expenses and a \$0.3 million decrease in expenses related to our vehicle fleet.



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Gross operating margin. The \$2.7 million decrease in Gross operating margin was primarily due to an increase in operating expenses during the six months ended June 30, 2016 and a decrease in revenues. The 1.3% decrease in Gross operating margin percentage from 70.9% for the six months ended June 30, 2015 to 69.6% for the six months ended June 30, 2016 was due in part to parts and service revenue consisting of a greater percentage of total revenue, which has lower margins.

Selling, general and administrative expense. The \$0.8 million increase in selling, general and administrative expense for the six months ended June 30, 2016 was primarily attributable to a \$2.6 million increase in unit-based compensation expense, offset by a \$1.7 million decrease in bad debt expense.

Depreciation and amortization expense. The \$3.3 million increase in depreciation and amortization expense was entirely related to an increase in gross property and equipment balances during the six months ended June 30, 2016 compared to gross balances during the six months ended June 30, 2015. There was no variance in amortization expense between the same periods, as intangible assets are amortized on a straight-line basis and there has been no change in gross identifiable intangible assets between the periods.

Loss (gain) on sale of assets. During the six months ended June 30, 2016 we transferred property and equipment and incurred a \$1.0 million loss associated with the portion of the property and equipment that was not transferable. The \$0.2 million gain on sale of assets during the six months ended June 30, 2015 was primarily attributable to a cash insurance recovery on previously impaired compression equipment received during the first quarter of 2015.

Impairment on compression equipment. The \$0.7 million and \$26.8 million impairment charge during the six months ended June 30, 2016 and 2015, respectively, resulted from our evaluation of the future deployment of our current idle fleet under the current market conditions. Our evaluation determined that due to certain performance characteristics of the impaired equipment, such as excessive maintenance costs and the inability of the equipment to meet current emission standards without retrofitting, this equipment was unlikely to be accepted by customers under current market conditions. As a result of our evaluation during the second quarter of 2016 and 2015, we determined to retire and either sell or re-utilize the key components of 5 and 166 compression units, respectively, with a total of approximately 1,700 and 58,000 horsepower, respectively, that had been previously used to provide compression services in our business.

Interest expense, net. The \$1.8 million increase in interest expense, net was primarily attributable to an increase in the weighted average interest rate. Our revolving credit facility bore an interest rate of 2.51% and 2.19% at June 30, 2016 and 2015, respectively, and a weighted average interest rate of 2.47% and 2.19% for the six months ended June 30, 2016 and 2015, respectively. Also contributing to the increase in interest expense was the impact of an approximate \$42.3 million increase in average outstanding borrowings under our revolving credit facility, for which average borrowings were \$742.4 million for the six months ended June 30, 2016 compared to \$700.1 million for the six months ended June 30, 2015.

Income tax expense. This line item represents the Revised Texas Franchise Tax. Approximately \$0.1 million of the increase in income tax expense for the six months ended June 30, 2016 compared to the six months ended June 30, 2015 was due to fluctuation in the deferred tax liability reflecting the book/tax basis difference in our property and equipment.

#### Other Financial Data

The following table summarizes other financial data for the periods presented (dollars in thousands):

Other Financial Data: (1)	Three Months Ended June 30,				Six Months Ended June 30,			
	2016	2015	Change		2016	2015	Change	
Gross operating margin	\$ 44,857	\$ 47,311	(5.2)	%	\$ 90,395	\$ 93,100	(2.9)	%
Gross operating margin percentage (2)	70.6	71.3	(0.9)	%	69.6	70.9	(1.8)	%
Adjusted EBITDA	\$ 37,149	\$ 38,618	(3.8)	%	\$ 75,553	\$ 76,136	(0.8)	%
Adjusted EBITDA percentage (2)	58.5	58.2	0.6	%	58.2	57.9	0.4	%
DCF (3)	\$ 30,490	\$ 31,001	(1.6)	%	\$ 62,403	\$ 60,381	3.3	%
DCF Coverage Ratio (3)	1.03	1.23	(16.2)	%	1.07	1.22	(12.3)	%
Cash Coverage Ratio	1.33	3.08	(56.7)	%	1.49	3.03	(50.9)	%

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- (1) Gross operating margin, Adjusted EBITDA, Distributable Cash Flow (“DCF”), DCF Coverage Ratio and Cash Coverage Ratio are all non-GAAP financial measures. Definitions of each measure, as well as reconciliations of each measure to its most directly comparable financial measure(s) calculated and presented in accordance with GAAP, can be found below under the caption “—Non-GAAP Financial Measures.”
- (2) Gross operating margin percentage and Adjusted EBITDA percentage are calculated as a percentage of revenue.
- (3) DCF and DCF Coverage Ratio were previously presented as Adjusted DCF and Adjusted DCF Coverage Ratio, respectively. The definitions of DCF and DCF Coverage Ratio are identical to the definition of Adjusted DCF and Adjusted DCF Coverage Ratio, respectively, as previously presented. Definitions of DCF and DCF Coverage Ratio can be found below under the caption “—Non-GAAP Financial Measures”.

Adjusted EBITDA. Adjusted EBITDA during the three months ended June 30, 2016 decreased \$1.5 million, or 3.8%, over the three months ended June 30, 2015, primarily due to a \$2.5 million decrease in Gross operating margin offset by \$1.0 million lower selling, general and administrative expenses, excluding unit-based compensation expense, during the three months ended June 30, 2016.

Adjusted EBITDA during the six months ended June 30, 2016 decreased \$0.6 million, or 0.8%, over the six months ended June 30, 2015, primarily due to a \$2.7 million decrease in Gross operating margin offset by \$1.7 million lower selling, general and administrative expenses, excluding unit-based compensation expense, during the six months ended June 30, 2016.

DCF. The decrease in DCF during the three months ended June 30, 2016 was primarily attributable to a \$2.5 million decrease in Gross operating margin along with \$0.6 million higher cash interest expense, net, offset by \$1.4 million lower maintenance capital expenditures and \$1.0 million lower selling, general and administrative expenses, excluding unit-based compensation expense during the comparable period.

The increase in DCF during the six months ended June 30, 2016 was primarily attributable to \$4.1 million lower maintenance capital expenditures and \$1.7 million lower selling, general and administrative expenses, excluding unit-based compensation expense, offset by a \$2.7 million decrease in Gross operating margin along with \$1.6 million higher cash interest expense, net, during the comparable period.

Coverage Ratios. The disproportionate decrease in Cash Coverage Ratio (as compared to DCF Coverage Ratio) is due to period to period decreases in DRIP participation by USA Compression Holdings and Argonaut Private Equity, L.L.C.

## Liquidity and Capital Resources

### Overview

We operate in a capital-intensive industry, and our primary liquidity needs are to finance the purchase of additional compression units and make other capital expenditures, service our debt, fund working capital, and pay distributions. Our principal sources of liquidity include cash generated by operating activities, borrowings under our revolving credit facility and issuances of debt and equity securities, including under the DRIP.

We believe cash generated by operating activities and, where necessary, borrowings under our revolving credit facility will be sufficient to service our debt, fund working capital, fund our estimated 2016 expansion capital expenditures, fund our maintenance capital expenditures and pay distributions. Because we distribute all of our available cash, which excludes prudent operating reserves, we expect to fund any future expansion capital expenditures or acquisitions primarily with capital from external financing sources, such as borrowings under our revolving credit facility and issuances of debt and equity securities, including under the DRIP.

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## Cash Flows

The following table summarizes our sources and uses of cash for the six months ended June 30, 2016 and 2015 as of the end of the periods presented (in thousands):

	Six Months Ended June 30,	
	2016	2015
Net cash provided by operating activities	\$ 58,457	\$ 48,550
Net cash used in investing activities	(24,644)	(182,399)
Net cash provided by (used in) financing activities	(33,813)	133,850

Net cash provided by operating activities. The \$9.9 million increase in net cash provided by operating activities for the six months ended June 30, 2016 relates primarily to a \$9.9 million decrease in inventory purchases and lower selling, general and administrative expenses, excluding unit-based compensation expense, offset by a slight decrease in Gross operating margin. Our significant reduction in compression unit purchases has reduced our serialized parts inventory requirements.

Net cash used in investing activities. Net cash used in investing activities for the six months ended June 30, 2016 and 2015 related primarily to purchases of new compression units, reconfiguration costs and related equipment. We have significantly reduced our purchases of new compression units during 2016 due to the slow-down in the overall energy market.

Net cash provided by (used in) financing activities. During the six months ended June 30, 2016, we borrowed \$5.9 million, on a net basis, primarily to support our purchases of new compression units, reconfiguration costs and related equipment, as described above. Additionally, we paid various loan fees and incurred costs in respect of our revolving credit facility in the amount of \$2.0 million and made cash distributions to our unitholders of \$37.6 million.

During the six months ended June 30, 2015, we borrowed, on a net basis, \$158.9 million primarily to support our purchases of new compression units, as described above, paid various loan fees and incurred costs in respect of our revolving credit facility in the amount of \$3.4 million and made cash distributions to our unitholders of \$21.5 million.

## Capital Expenditures

The compression services business is capital intensive, requiring significant investment to maintain, expand and upgrade existing operations. Our capital requirements have consisted primarily of, and we anticipate that our capital requirements will continue to consist primarily of, the following:

- maintenance capital expenditures, which are capital expenditures made to maintain the operating capacity of our assets and extend their useful lives, to replace partially or fully depreciated assets, or other capital expenditures that are incurred in maintaining our existing business and related operating income; and
- expansion capital expenditures, which are capital expenditures made to expand the operating capacity or operating income capacity of assets, including by acquisition of compression units or through modification of existing compression units to increase their capacity, or to replace certain partially or fully depreciated assets that were not currently generating operating income.

We classify capital expenditures as maintenance or expansion on an individual asset basis. Over the long term, we expect that our maintenance capital expenditure requirements will increase as either, or both of, the overall size and age of our fleet increases. Our aggregate maintenance capital expenditures for the six months ended June 30, 2016 and 2015 were \$3.0 million and \$7.2 million, respectively. We currently plan to spend approximately \$10.5 million in maintenance capital expenditures during 2016.

Without giving effect to any equipment we may acquire pursuant to any future acquisitions, we currently have budgeted between \$40 million and \$50 million in expansion capital expenditures during 2016. Our expansion capital

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expenditures for the six months ended June 30, 2016 and 2015 were \$18.5 million (of which a majority related to payments for prior year purchases) and \$176.8 million, respectively. As of June 30, 2016, we had binding commitments to purchase \$7.2 million of additional units and serialized parts, which we expect to be delivered in the remainder of 2016.

### Revolving Credit Facility

As of June 30, 2016, we were in compliance with all of our covenants under our revolving credit facility. As of June 30, 2016, we had outstanding borrowings under our revolving credit facility of \$735.1 million, \$364.9 million of borrowing base availability and, subject to compliance with the applicable financial covenants, available borrowing capacity of \$146.0 million.

As of August 2, 2016, we had outstanding borrowings under our revolving credit facility of \$740.6 million.

For a more detailed description of our revolving credit facility, please see Note 7 to the unaudited condensed consolidated financial statements under Part I, Item 1 of this report and Note 8 to the consolidated financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2015 filed on February 11, 2016 (our “2015 Annual Report”).

### Distribution Reinvestment Plan

During the six months ended June 30, 2016, distributions of \$21.3 million were reinvested under the DRIP resulting in the issuance of 2.1 million common units. Such distributions are treated as non-cash transactions in the accompanying Unaudited Condensed Consolidated Statements of Cash Flows included under Part I, Item 1 of this report.

For a more detailed description of the DRIP, please see Note 8 to our unaudited condensed consolidated financial statements under Part I, Item 1 of this report and Note 9 to the consolidated financial statements included in our 2015 Annual Report.

### Non-GAAP Financial Measures

## Gross Operating Margin

Gross operating margin is a non-GAAP financial measure. We define Gross operating margin as revenue less cost of operations, exclusive of depreciation and amortization expense. We believe that Gross operating margin is useful as a supplemental measure of our operating profitability. Gross operating margin is impacted primarily by the pricing trends for service operations and cost of operations, including labor rates for service technicians, volume and per unit costs for lubricant oils, quantity and pricing of routine preventative maintenance on compression units and property tax rates on compression units. Gross operating margin should not be considered an alternative to, or more meaningful than, operating income or any other measure of financial performance presented in accordance with GAAP. Moreover, Gross operating margin as presented may not be comparable to similarly titled measures of other companies. Because we capitalize assets, depreciation and amortization of equipment is a necessary element of our costs. To compensate for the limitations of Gross operating margin as a measure of our performance, we believe that it is important to consider operating income determined under GAAP, as well as Gross operating margin, to evaluate our operating profitability.



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The following table reconciles Gross operating margin to operating income, its most directly comparable GAAP financial measure, for each of the periods presented (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Revenues:				
Contract operations	\$ 62,785	\$ 65,552	\$ 127,063	\$ 129,587
Parts and service	726	838	2,815	1,803
Total revenues	63,511	66,390	129,878	131,390
Cost of operations, exclusive of depreciation and amortization	18,654	19,079	39,483	38,290
Gross operating margin	44,857	47,311	90,395	93,100
Other operating and administrative costs and expenses:				
Selling, general and administrative	11,180	10,350	20,919	20,079
Depreciation and amortization	23,412	21,507	45,506	42,238
Loss (gain) on sale of assets	1,072	(23)	950	(218)
Impairment of compression equipment	693	26,829	693	26,829
Total other operating and administrative costs and expenses	36,357	58,663	68,068	88,928
Operating income (loss)	\$ 8,500	\$ (11,352)	\$ 22,327	\$ 4,172

## Adjusted EBITDA

We define EBITDA as net income (loss) before net interest expense, depreciation and amortization expense, and income taxes. We define Adjusted EBITDA as EBITDA plus impairment of compression equipment, impairment of goodwill, interest income on capital lease, unit-based compensation expense, severance charges, certain transaction fees, and loss (gain) on sale of assets and other. We view Adjusted EBITDA as one of our primary management tools, and we track this item on a monthly basis both as an absolute amount and as a percentage of revenue compared to the prior month, year-to-date, prior year and to budget. Adjusted EBITDA is used as a supplemental financial measure by our management and external users of our financial statements, such as investors and commercial banks, to assess:

- the financial performance of our assets without regard to the impact of financing methods, capital structure or historical cost basis of our assets;
- the viability of capital expenditure projects and the overall rates of return on alternative investment opportunities;

- the ability of our assets to generate cash sufficient to make debt payments and to make distributions; and
- our operating performance as compared to those of other companies in our industry without regard to the impact of financing methods and capital structure.

We believe that Adjusted EBITDA provides useful information to investors because, when viewed with our GAAP results and the accompanying reconciliations, it provides a more complete understanding of our performance than GAAP results alone. We also believe that external users of our financial statements benefit from having access to the same financial measures that management uses in evaluating the results of our business.

Adjusted EBITDA should not be considered an alternative to, or more meaningful than, net income (loss), operating income, cash flows from operating activities or any other measure of financial performance presented in accordance with GAAP as measures of operating performance and liquidity. Moreover, our Adjusted EBITDA as presented may not be comparable to similarly titled measures of other companies.

Because we use capital assets, depreciation and the interest cost of acquiring compression equipment are also necessary elements of our costs. Expense related to unit-based compensation expense related to equity awards to employees is also a necessary component of our business. Therefore, measures that exclude these elements have

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material limitations. To compensate for these limitations, we believe that it is important to consider both net income (loss) and net cash provided by operating activities determined under GAAP, as well as Adjusted EBITDA, to evaluate our financial performance and our liquidity. Our Adjusted EBITDA excludes some, but not all, items that affect net income (loss) and net cash provided by operating activities, and these measures may vary among companies. Management compensates for the limitations of Adjusted EBITDA as an analytical tool by reviewing the comparable GAAP measures, understanding the differences between the measures and incorporating this knowledge into management's decision making processes.

The following table reconciles Adjusted EBITDA to net income (loss) and net cash provided by operating activities, its most directly comparable GAAP financial measures, for each of the periods presented (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Net income (loss)	\$ 3,274	\$ (15,904)	\$ 11,812	\$ (4,448)
Interest expense, net	5,139	4,415	10,201	8,409
Depreciation and amortization	23,412	21,507	45,506	42,238
Income taxes	94	142	328	221
EBITDA	\$ 31,919	\$ 10,160	\$ 67,847	\$ 46,420
Impairment of compression equipment	693	26,829	693	26,829
Interest income on capital lease	362	414	737	841
Unit-based compensation expense (1)	3,022	1,238	4,834	2,264
Severance charges	81	—	492	—
Loss (gain) on sale of assets	1,072	(23)	950	(218)
Adjusted EBITDA	\$ 37,149	\$ 38,618	\$ 75,553	\$ 76,136
Interest expense, net	(5,139)	(4,415)	(10,201)	(8,409)
Income tax expense	(94)	(142)	(328)	(221)
Interest income on capital lease	(362)	(414)	(737)	(841)
Non-cash interest expense	548	415	1,015	870
Severance charges	(81)	—	(492)	—
Changes in operating assets and liabilities	4,476	(25)	(6,353)	(18,985)
Net cash provided by operating activities	\$ 36,497	\$ 34,037	\$ 58,457	\$ 48,550

(1) For the three and six months ended June 30, 2016, unit-based compensation expense included \$0.7 million and \$1.5 million, respectively, of cash payments related to quarterly payments of distribution equivalent rights on phantom unit awards and, for the six months ended June 30, 2016, \$0.1 million related to the cash portion of any settlement of phantom unit awards upon vesting. For the three and six months ended June 30, 2015, unit-based compensation expense included \$0.2 million and \$0.4 million, respectively, of cash payments related to quarterly payments of distribution equivalent rights on phantom unit awards and, for the six months ended June 30, 2015, \$0.2 million related to the cash portion of any settlement of phantom unit awards upon vesting. The remainder of the unit-based compensation expense for both periods was related to non-cash adjustments to the unit-based compensation liability.

Distributable Cash Flow

We define DCF as net income (loss) plus non-cash interest expense, non-cash income tax expense, depreciation and amortization expense, unit-based compensation expense, severance charges, impairment of compression equipment, impairment of goodwill, certain transaction fees and loss (gain) on sale of assets and other, less maintenance capital expenditures. The definition of DCF is identical to the definition of Adjusted DCF previously presented. We believe DCF is an important measure of operating performance because it allows management, investors and others to compare basic cash flows we generate (prior to the establishment of any retained cash reserves by our general partner and the effect of the DRIP) to the cash distributions we expect to pay our unitholders. Using DCF, management can quickly compute the coverage ratio of estimated cash flows to planned cash distributions.

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DCF should not be considered as an alternative to, or more meaningful than, net income (loss), operating income, cash flows from operating activities or any other measure of financial performance presented in accordance with GAAP as measures of operating performance and liquidity. Moreover, our DCF as presented may not be comparable to similarly titled measures of other companies.

Because we use capital assets, depreciation, loss (gain) on sale of assets, and maintenance capital expenditures are necessary elements of our costs. Expense related to unit-based compensation expense related to equity awards to employees is also a necessary component of our business. Therefore, measures that exclude these elements have material limitations. To compensate for these limitations, we believe that it is important to consider both net income (loss) and net cash provided by operating activities determined under GAAP, as well as DCF, to evaluate our financial performance and our liquidity. Our DCF excludes some, but not all, items that affect net income (loss) and net cash provided by operating activities, and these measures may vary among companies. Management compensates for the limitations of DCF as an analytical tool by reviewing the comparable GAAP measures, understanding the differences between the measures and incorporating this knowledge into management's decision making processes.

The following table reconciles DCF to net income (loss) and net cash provided by operating activities, its most directly comparable GAAP financial measures, for each of the periods presented (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Net income (loss)	\$ 3,274	\$ (15,904)	\$ 11,812	\$ (4,448)
Plus: Non-cash interest expense	548	415	1,015	870
Plus: Non-cash income tax expense	32	—	134	—
Plus: Depreciation and amortization	23,412	21,507	45,506	42,238
Plus: Unit-based compensation expense (1)	3,022	1,238	4,834	2,264
Plus: Severance charges	81	—	492	—
Plus: Loss (gain) on sale of assets	1,072	(23)	950	(218)
Plus: Impairment of compression equipment	693	26,829	693	26,829
Less: Maintenance capital expenditures (2)	(1,644)	(3,061)	(3,033)	(7,154)
DCF (3)	\$ 30,490	\$ 31,001	\$ 62,403	\$ 60,381
Plus: Maintenance capital expenditures	1,644	3,061	3,033	7,154
Plus: Changes in operating assets and liabilities	4,476	(25)	(6,353)	(18,985)
Less: Other	(113)	—	(626)	—
Net cash provided by operating activities	\$ 36,497	\$ 34,037	\$ 58,457	\$ 48,550

(1) For the three and six months ended June 30, 2016, unit-based compensation expense included \$0.7 million and \$1.5 million, respectively, of cash payments related to quarterly payments of distribution equivalent rights on phantom unit awards and, for the six months ended June 30, 2016, \$0.1 million related to the cash portion of any settlement of phantom unit awards upon vesting. For the three and six months ended June 30, 2015, unit-based compensation expense included \$0.2 million and \$0.4 million, respectively, of cash payments related to quarterly

payments of distribution equivalent rights on phantom unit awards and, for the six months ended June 30, 2015, \$0.2 million related to the cash portion of any settlement of phantom unit awards upon vesting. The remainder of the unit-based compensation expense for both periods was related to non-cash adjustments to the unit-based compensation liability.

- (2) Reflects actual maintenance capital expenditures for the period presented. Maintenance capital expenditures are capital expenditures made to replace partially or fully depreciated assets, to maintain the operating capacity of our assets and extend their useful lives, or other capital expenditures that are incurred in maintaining our existing business and related cash flow.
- (3) DCF was previously presented as Adjusted DCF.

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## Coverage Ratios

DCF Coverage Ratio is defined as DCF less cash distributions to our general partner and IDRs, divided by distributions declared to limited partner unitholders for the period. Cash Coverage Ratio is defined as DCF less cash distributions to our general partner and IDRs divided by cash distributions paid to limited partner unitholders, after taking into account the non-cash impact of the DRIP. We believe DCF Coverage Ratio and Cash Coverage Ratio are important measures of operating performance because they allow management, investors and others to gauge our ability to pay cash distributions to limited partner unitholders using the cash flows that we generate. Our DCF Coverage Ratio and Cash Coverage Ratio as presented may not be comparable to similarly titled measures of other companies.

The following table summarizes certain coverage ratios for the periods presented (dollars in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
DCF (1)	\$ 30,490	\$ 31,001	\$ 62,403	\$ 60,381
General partner interest in DCF	715	671	1,426	1,219
DCF attributable to limited partner interest	\$ 29,775	\$ 30,330	\$ 60,977	\$ 59,162
Distributions for DCF Coverage Ratio (2)	\$ 28,805	\$ 24,579	\$ 57,238	\$ 48,358
Distributions reinvested in the DRIP (3)	\$ 6,483	\$ 14,731	\$ 16,290	\$ 28,842
Distributions for Cash Coverage Ratio (4)	\$ 22,322	\$ 9,848	\$ 40,948	\$ 19,516
DCF Coverage Ratio	1.03	1.23	1.07	1.22
Cash Coverage Ratio	1.33	3.08	1.49	3.03

(1) DCF was previously presented as Adjusted DCF.

(2) Represents distributions to the holders of the Partnership's common units as of the record date.

(3) Represents distributions to holders enrolled in the DRIP as of the record date. The amount for the three and six months ended June 30, 2016 is based on an estimate as of the record date.

(4) Represents cash distributions declared for common units not participating in the DRIP.

## Off-Balance Sheet Arrangements

We have no off-balance sheet financing activities.

## Recent Accounting Pronouncement

For discussion on specific recent accounting pronouncements affecting us, please see Note 11 to our unaudited condensed consolidated financial statements under Part I, Item 1 of this report.

## ITEM 3. Quantitative and Qualitative Disclosures About Market Risk

### Commodity Price Risk

Market risk is the risk of loss arising from adverse changes in market rates and prices. We do not take title to any natural gas or crude oil in connection with our services and, accordingly, have no direct exposure to fluctuating commodity prices. However, the demand for our compression services depends upon the continued demand for, and production of, natural gas and crude oil. Natural gas or crude oil prices remaining low over the long term could result in a continued decline in the production of natural gas or crude oil, which could result in further reduced demand for our

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compression services. We do not intend to hedge our indirect exposure to fluctuating commodity prices. A 1% decrease in average revenue generating horsepower of our active fleet during the six months ended June 30, 2016 would have resulted in a decrease of approximately \$2.6 million and \$1.8 million in our revenue and Gross operating margin, respectively. Gross operating margin is a non-GAAP financial measure. For a reconciliation of Gross operating margin to net income, its most directly comparable financial measure, calculated and presented in accordance with GAAP, please read “Part I, Item 2 Management’s Discussion and Analysis of Financial Condition and Results of Operations—Non-GAAP Financial Measures” of this report.

## Interest Rate Risk

We are exposed to market risk due to variable interest rates under our financing arrangements.

As of June 30, 2016, we had approximately \$735.1 million of variable-rate outstanding indebtedness at a weighted-average interest rate of 2.47%. A 1% increase or decrease in the effective interest rate on our variable-rate outstanding debt at June 30, 2016 would have resulted in an annual increase or decrease in our interest expense of approximately \$7.4 million.

For further information regarding our exposure to interest rate fluctuations on our debt obligations see Note 7 to our unaudited condensed consolidated financial statements under Part I, Item 1 of this report. Although we do not currently hedge our variable rate debt, we may, in the future, hedge all or a portion of such debt.

## Credit Risk

Our credit exposure generally relates to receivables for services provided. If any significant customer of ours should have credit or financial problems resulting in a delay or failure to repay the amount it owes us, it could have a material adverse effect on our business, financial condition, results of operations or cash flows.

## ITEM 4. Controls and Procedures

### Management’s Evaluation of Disclosure Controls and Procedures

As required by Rule 13a-15(b) of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), we have evaluated, under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of the period covered by this report. Our disclosure controls and procedures are designed to provide reasonable assurance that the information required to be disclosed by us in reports that we file under the Exchange Act is accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosures, and is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the SEC. Based upon the evaluation, our principal executive officer and principal financial officer have concluded that our disclosure controls and procedures were effective as of June 30, 2016 at the reasonable assurance level.

#### Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) during the last fiscal quarter that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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PART II. OTHER INFORMATION

ITEM 1. Legal Proceedings

From time to time, we may be involved in various legal or governmental proceedings and litigation arising in the ordinary course of business. In management's opinion, the resolution of such matters is not expected to have a material adverse effect on our consolidated financial position, results of operations or cash flows.

ITEM 1A. Risk Factors

Security holders and potential investors in our securities should carefully consider the risk factors below and set forth in Part I, "Item 1A. Risk Factors" of our 2015 Annual Report. We have identified these risk factors as important factors that could cause our actual results to differ materially from those contained in any written or oral forward-looking statements made by us or on our behalf.

New federal regulations of methane and volatile organic compound emissions under the Clean Air Act could result in increased compliance costs.

On June 3, 2016, the Environmental Protection Agency ("EPA") issued a package of final rules under the Clean Air Act directed at the oil and gas industry. The EPA's rule package included New Source Performance Standards establishing regulations for methane and volatile organic compound ("VOC") emissions from certain "facilities" in the oil and gas sector that are new, modified, or reconstructed after September 18, 2015. The new rule mandates that control devices or practices be used to reduce methane and VOC emissions from certain equipment used in our operations by 95% starting in August 2016. The rule also imposes fugitive emission leak detection and repair requirements on certain well sites and compressor stations beginning in June 2017. This rule will require a number of changes to those parts of our operations that are, or in the future become, subject to these requirements, including modifying equipment to control emissions, and additional monitoring and recordkeeping requirements for both the equipment and compressor stations that we own or operate. We may not be able to pass on all of the increased costs associated with these regulations to our customers. While we do not think we are situated any differently than our competitors with regards to these rules, compliance with such rules may result in significant costs, including increased capital expenditures and operating costs, and could adversely impact our business.

ITEM 6. Exhibits

The documents in the accompanying Exhibit Index are filed, furnished or incorporated by reference as part of this report and such Exhibit Index is incorporated herein by reference.

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SIGNATURES

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

August 4, 2016 USA Compression Partners, LP

By: USA Compression GP, LLC  
its General Partner

By: /s/ Matthew C. Liuzzi  
Vice President, Chief Financial Officer and Treasurer  
(Principal Financial Officer)

By: /s/ Michael D. Lenox  
Vice President- Finance and Chief Accounting Officer  
(Principal Accounting Officer)

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EXHIBIT INDEX

Exhibit No.	Description
3.1	Certificate of Limited Partnership of USA Compression Partners, LP (incorporated by reference to Exhibit 3.1 to Amendment No. 3 of the Partnership's registration statement on Form S-1 (Registration No. 333-174803) filed on December 21, 2011)
3.2	First Amended and Restated Agreement of Limited Partnership of USA Compression Partners, LP (incorporated by reference to Exhibit 3.1 to the Partnership's Current Report on Form 8-K (File No. 001-35779) filed on January 18, 2013)
31.1	* Certification of Chief Executive Officer pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934
31.2	* Certification of Chief Financial Officer pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934
32.1	# Certification of 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
101.1	* Interactive data files pursuant to Rule 405 of Regulation S-T

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\*Filed herewith.

#Furnished herewith. Not considered to be "filed" for the purposes of Section 18 of the Securities Exchange Act of 1934 or otherwise subject to the liabilities of that section.