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HALLADOR PETROLEUM CO
Form 10QSB
November 14, 2003

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

FORM 10-QSB

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

For the quarterly period ended September 30, 2003

OR

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

Commission File Number 0-14731

HALLADOR PETROLEUM COMPANY
(Exact name of registrant as specified in its charter)

Colorado
(State of incorporation)

84-1014610
(I.R.S. Employer Identification No.)

1660 Lincoln Street, Suite 2700, Denver, Colorado 80264-2701
(Address of principal executive offices)

303-839-5504

(Issuer's telephone numbers)

FAX: 303-832-3013

Check whether the issuer (1) filed all reports required by Section 13 or 15(d)
of the Securities Exchange Act during the past 12 months, and (2) has been
subject to such filing requirements for the past 90 days: Yes No

Shares outstanding as of November 14, 2003: 7,093,150

PART I - FINANCIAL INFORMATION

Consolidated Balance Sheet
(in thousands)

September 30, 2003	December 31, 2002*
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ASSETS

Current assets:

Cash and cash equivalents	\$ 4,220	\$ 1,647
Accounts receivable-		
Oil and gas sales	569	680
Well operations	306	146
	-----	-----
Total current assets	5,095	2,473
	-----	-----

Oil and gas properties, at cost (successful efforts):

Unproved properties	364	247
Proved properties	26,047	25,058
Less - accumulated depreciation, depletion, amortization and impairment	(19,556)	(18,836)
	-----	-----
	6,855	6,469
	-----	-----

Oil and gas operator bonds	507	417
Investment in Catalytic Solutions	164	164
Other assets	34	38
	-----	-----
	\$12,655	\$ 9,561
	=====	=====

LIABILITIES AND STOCKHOLDERS' EQUITY

Current liabilities:

Accounts payable and accrued liabilities	\$ 2,508	\$ 527
Oil and gas sales payable	266	185
	-----	-----
Total current liabilities	2,774	712
	-----	-----

Bank debt		251

Key employee bonus plan	236	209
	-----	-----
Future site restoration-South Cuyama Field	974	653
	-----	-----
Minority interest	5,043	4,763
	-----	-----

Commitments and contingencies

Stockholders' equity:

Preferred stock, \$.10 par value; 10,000,000 shares authorized; none issued		
Common stock, \$.01 par value; 100,000,000 shares authorized, 7,093,150 shares issued	71	71
Additional paid-in capital	18,061	18,061
Accumulated deficit	(14,504)	(15,159)
	-----	-----
	3,628	2,973
	-----	-----
	\$12,655	\$ 9,561
	=====	=====

*Derived from the Form 10-KSB.

See accompanying notes.

Consolidated Statement of Operations
(in thousands)

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	Nine months ended		Three months ended	
	September 30,		September 30,	
	2003	2002	2003	2002
	-----	-----	-----	-----
Revenue:				
Oil	\$5,686	\$4,813	\$1,858	\$1,933
Gas	1,296	858	461	298
Crude oil class action settlement	153		153	
Interest and other	117	35	8	10
	-----	-----	-----	-----
	7,252	5,706	2,480	2,241
	-----	-----	-----	-----
Costs and expenses:				
Lease operating	3,963	3,474	1,232	1,208
Exploration costs -				
Geological and geophysical	64	1,031		1,031
Dry hole	223		223	
Plug and abandonment	42		42	
Delay rentals	106	55	44	9
Unproved properties	19			
Impairments -				
Fulton Fuller gas well		79		
S.E. Bonus Field		840		
Unproved properties		18		18
Depreciation, depletion and amortization	868	1,918	306	572
General and administrative	850	640	265	190
	-----	-----	-----	-----
	6,135	8,055	2,112	3,028
	-----	-----	-----	-----
Income (loss) before cumulative effect of change in accounting principle	1,117	(2,349)	368	(787)
Cumulative effect of change in accounting principle	(181)			
	-----	-----	-----	-----
Income (loss) before minority interest	936	(2,349)	368	(787)
Minority interest	(281)	705	(110)	236
	-----	-----	-----	-----
Net income (loss)	\$ 655	\$ (1,644)	\$ 258	\$ (551)
	=====	=====	=====	=====
Income (loss) per share-basic and diluted:				
Before cumulative effect of change in accounting principle	\$.11	\$ (.23)	\$.04	\$ (.08)
Cumulative effect of change in accounting principle	(.02)			
	-----	-----	-----	-----
Net income (loss)	\$.09	\$ (.23)	\$.04	\$ (.08)
	=====	=====	=====	=====
Weighted average shares outstanding-basic	7,093	7,093	7,093	7,093
	=====	=====	=====	=====

See accompanying notes.

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Consolidated Statement of Cash Flows (in thousands)

	Nine months ended September 30,	
	2003	2002
	-----	-----
Net cash provided by operating activities	\$2,893	\$1,206
	-----	-----
Cash flows from investing activities:		
Properties	(945)	(993)
Operator bonds	(91)	(53)
	-----	-----
Net cash used in investing activities	(1,036)	(1,046)
	-----	-----
Cash flows from financing activities:		
Debt retirement	(251)	
Cash calls from joint interest owners	967	

Net cash from financing activities	716	

Net increase in cash and cash equivalents	2,573	160
Cash and cash equivalents, beginning of period	1,647	2,078
	-----	-----
Cash and cash equivalents, end of period	\$ 4,220	\$2,238
	=====	=====

See accompanying notes.

Notes to Financial Statements

1. The interim financial data is unaudited; however, in our opinion, it includes all adjustments, consisting only of normal recurring adjustments necessary for a fair statement of the results for the interim periods. The financial statements included herein have been prepared pursuant to the SEC's rules and regulations; accordingly, certain information and footnote disclosures normally included in GAAP financial statements have been condensed or omitted.

2. Our organization and business, the accounting policies we follow and other information are contained in the notes to our financial statements filed as part of our 2002 Form 10-KSB. This quarterly report should be read in conjunction with that annual report.

3. In July 2001, the Financial Accounting Standards Board issued SFAS No. 143, "Accounting for Asset Retirement Obligations." SFAS No. 143 requires entities to record the fair value of a liability for an asset retirement obligation in the period in which it is incurred and a corresponding increase in the carrying amount of the related long-lived asset and is effective for fiscal years beginning after June 15, 2002. We adopted SFAS No. 143 on January 1, 2003 and increased our liability for asset retirement obligations by \$264,000 (using an 8% discount rate) and recorded a cumulative effect of change in accounting principle of \$181,000. For the nine months ended September 30, 2003, we recognized \$56,000 of accretion on the liability as a component of depletion expense.

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Had SFAS No. 143 been adopted on January 1, 2002, the pro forma net loss would have been \$1,725,000 and the pro forma net loss per share would have been \$(.24) for the nine months ended September 30, 2002 and the pro forma asset retirement obligation at January 1, 2002 would have been \$850,000.

4. As allowed in SFAS No. 123, "Accounting for Stock-Based Compensation," we continue to apply Accounting Principles Board Opinion (APB) No. 25, "Accounting for Stock Issued to Employees," and related interpretations in recording compensation related to our plan. The pro forma effect on our net income (loss) was not material for any of the periods presented. No grants were issued during the first nine months of 2003.

5. As discussed in previous filings, the SC Field was purchased from ARCO (Atlantic Richfield which is now part of BP p.l.c.) in May 1990. As part of the Purchase and Sale Agreement, ARCO agreed to indemnify us for certain environmental liabilities connected with their 40-year ownership of the field and gas plant ("ARCO Indemnity"). Part of the gas plant has not been operational during the past twenty-five years. There is evidence of asbestos in the non-operational part of the gas plant. It is our position, and the opinion of our legal counsel, that the ARCO Indemnity covers future abandonment and clean-up costs associated with this gas plant. We have had several discussions with BP regarding this matter and have retained a San Francisco law firm to assert our rights under the ARCO Indemnity. BP continues to deny any responsibility.

The costs to abandon and clean up the gas plant area and other oil and gas areas at the field will be significant. There is a chance, depending on the negotiations and legal proceedings with BP, that some or all of the costs could be borne by us. At this time we are unable to estimate what these costs could ultimately be but we expect that such costs could have a material adverse effect on our financial condition, results of operations and cash flows.

HALLADOR PETROLEUM COMPANY Management's Discussion and Analysis or Plan of Operation

RESULTS OF OPERATIONS

YEAR-TO-DATE COMPARISON

The table below (in thousands) provides sales data and average prices for the period.

	2003			2002		
	Sales Volume	Average Price	Revenue	Sales Volume	Average Price	Revenue
Oil - barrels						
South Cuyama field	194	\$28.66	\$5,560	210	\$22.34	\$4,692
Other	6	21.00	126	7	17.31	121
Gas - mcf						
South Cuyama field	135	5.39	728	80	3.14	251
San Juan-New Mexico	43	4.51	194	38	2.00	76
Other	63	5.93	374	181	2.93	531

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Oil revenue increased primarily due to higher prices as set forth in the table above. Gas revenue increased due to higher prices and production, even though there was a significant production decline in our South Texas - Bonus field. As previously disclosed, we took an impairment charge of \$840,000 in the second quarter of 2002 for this field.

During 1999 we agreed to participate in a class action suit against certain purchasers of crude oil in the state of California covering 1986 through 1998. The case was settled during the third quarter of 2003 and our share of the judgment, after contingent legal fees, was approximately \$153,000.

Current prices for the South Cuyama field are about \$27.40 for oil and \$4.74 for gas and San Juan gas is about \$4.60.

The table below (in thousands) shows lease operating expenses (LOE) for our two primary fields.

	2003	2002
	----	----
South Cuyama field:		
LOE excluding electricity	\$2,761	\$2,054
Electricity	1,152	1,221
Electricity refund	(115)	
	-----	-----
	3,798	3,275
San Juan-New Mexico	87	49
Other	78	150
	-----	-----
	\$3,963	\$3,474
	=====	=====

LOE in the field increased due to higher operating expenses relating to the new equipment we had to install in the first quarter of 2003 in order to remove CO2 from our gas stream. Furthermore, when oil prices are high, we perform more repair and maintenance in the field compared to when prices are low (see the table above for 2003 and 2002 average oil prices.)

The \$64,000 in G&G costs relate to a late billing for the 3-D work performed in the fourth quarter of 2002. The \$223,000 in dry hole expense relates to the dry hole drilled in the SC Field in the third quarter of this year. In addition we spent \$42,000 to properly plug and abandon a well in southern Colorado, which was drilled by our predecessor over 20 years ago. Delay rentals increased due to exploration activity we are planning next year on leases we acquired near the SC Field. These sites were identified by the 3-D project we performed last year.

The increase in G&A was due to higher 2002 audit and tax fees - \$35,000, accruals for 2003 audit and tax fees - \$25,000, state taxes - \$43,000, higher employee costs - \$50,000, higher legal fees associated with the ARCO Indemnity and SOCAL negotiations - \$24,000, donations - \$13,000, and other minor increases of \$20,000.

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DD&A decreased due to higher reserve estimates at September 30, 2003 compared to September 30, 2002. The increase in reserves was due to higher oil prices.

QUARTER-TO-DATE COMPARISON

The table below (in thousands) provides sales data and average prices for the period.

	2003			2002		
	Sales Volume	Average Price	Revenue	Sales Volume	Average Price	Revenue
Oil - barrels						
South Cuyama field	65	\$27.90	\$1,814	75	\$25.29	\$1,897
Other	2	22.00	44	1.6	22.50	36
Gas - mcf						
South Cuyama field	56	5.16	289	30	3.53	106
San Juan-New Mexico	17	4.41	75	11	2.36	26
Other	18	5.38	97	54	3.07	166

The table below (in thousands) shows lease operating expenses (LOE) for our primary fields.

	2003	2002
South Cuyama field:		
LOE excluding electricity	\$ 860	\$ 637
Electricity	458	504
Electricity refund	(115)	
	1,203	1,141
San Juan-New Mexico	8	18
Other	21	49
	\$1,232	\$1,208
	=====	=====

For the most part, the explanations above for the year-to-date comparisons also apply to the quarter-to-date comparisons.

LIQUIDITY AND CAPITAL RESOURCES

Cash and cash flow from operations are expected to enable us to meet our obligations as they become due during the next several years.

Bank Debt

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The SC Field, our principal asset, is pledged to U. S. Bank National Association under a \$2,200,000 revolving line of credit which was renewed on March 31, 2002. At March 31, 2003 we owed \$244,000 under this line. On April 28, 2003 the loan was paid off.

THE FOLLOWING DISCUSSION UPDATES THE MD&A CONTAINED IN ITEM 6 OF THE 2002 FORM 10-KSB AND THE TWO DISCUSSIONS SHOULD BE READ TOGETHER.

PROSPECT DEVELOPMENT AND EXPLORATION ACTIVITY

South Cuyama Field

Based on the results of our 2002 3-D project we have identified four wildcat sites located outside the field boundaries. Also, we have identified six developmental drilling opportunities within the boundaries of the field. During July 2003 we drilled three gas wells; one was a dry hole, one was successful and the other was marginal. It is too early to assign reserves to these wells, but the results are encouraging. The wildcat wells outside the field will not be drilled until sometime next year and no further development drilling is planned for this year.

Of the 63 oil wells in the field, five account for 60% of the oil production. Two gas wells account for 90% of the gas production. Due to air quality regulations in Santa Barbara County we began a project to electrify the field. This project began seven years ago, and all but one oil and gas well is electrified. Although we have higher electricity costs, the repairs and maintenance expenses are lower because electrical engines are much cheaper to maintain than combustion engines.

SOCAL

Currently gas sales in the SC Field are 1,000 MCF per day. Southern California Gas Company (SOCAL), the pipeline company and our only outlet to sell gas has imposed a 1,000 MCF per day maximum limit. If it weren't for this limit, we believe we could sell 2,500 MCF per day. If we are unable to sell more gas, we will have to curtail our exploration and development plans. We have been negotiating with SOCAL to increase the capacity from 1,000 MCF per day to 3,000 MCF per day. Recent negotiations with SOCAL have proved fruitless, and we don't know when and if our capacity will increase. Our gas reserves should last for at least 8 years producing at this low rate of 1,000 MCF per day. Considering the time value of money, we would much rather be producing at a much higher rate.

ARCO Indemnity

As discussed in previous filings, the SC Field was purchased from ARCO (Atlantic Richfield which is now part of BP p.l.c.) in May 1990. As part of the Purchase and Sale Agreement, ARCO agreed to indemnify us for certain environmental liabilities connected with their 40-year ownership of the field and gas plant ("ARCO Indemnity"). Part of the gas plant has not been operational during the past twenty-five years. There is evidence of asbestos in the non-operational part of the gas plant. It is our position, and the opinion of our legal counsel, that the ARCO Indemnity covers future abandonment and clean-up costs associated with this gas plant. We have had several discussions with BP regarding this matter and have retained a San Francisco law firm to assert our rights under the ARCO Indemnity. BP continues to deny any responsibility.

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The costs to abandon and clean up the gas plant area and other oil and gas areas at the field will be significant. There is a chance, depending on the negotiations and legal proceedings with BP, that some or all of the costs could be borne by us. At this time we are unable to estimate what these costs could ultimately be but we expect that such costs could have a material adverse effect on our financial condition, results of operations and cash flows.

San Juan Basin - New Mexico

Two successful development gas wells were drilled during April. During the third quarter we drilled four more successful development gas wells. These six wells cost about \$3.6 million to the 100%. We have an approximate 10% WI in these six wells. We expect to assign proved developed gas reserves to the 100% of between 1 BCF and 1.5 BCF per well. Our net revenue interest in these wells is about 8%. No more drilling is planned for the near future.

Predecessor Entity

Over the past 12 years we have paid about \$250,000 to properly plug and abandon 12 or so sites which were previously plugged and abandoned by Kimbark Oil & Gas Company, our predecessor entity. For the quarter ended September 30, 2003, we spent \$42,000 to properly plug and abandon a well in southern Colorado, which was drilled by our predecessor over 20 years ago. We do not expect any more notices from state regulatory jurisdictions regarding improperly P&A wells, but it is possible that there could be more.

SFAS No. 143 - "Accounting for Asset Retirement Obligations"

In July 2001, the Financial Accounting Standards Board issued SFAS No. 143, "Accounting for Asset Retirement Obligations." SFAS No. 143 requires entities to record the fair value of a liability for an asset retirement obligation in the period in which it is incurred and a corresponding increase in the carrying amount of the related long-lived asset and is effective for fiscal years beginning after June 15, 2002. We adopted SFAS No. 143 on January 1, 2003 and increased our liability for asset retirement obligations by \$264,000 (using an 8% discount rate) and recorded a cumulative effect of change in accounting principle of \$181,000. For the nine months ended September 30, 2003, we recognized \$56,000 of accretion on the liability as a component of depletion expense.

There are no other significant changes or developments to report from what we disclosed in the 2002 Form 10-KSB.

ITEM 3. CONTROLS AND PROCEDURES

We maintain a system of disclosure controls and procedures that are designed for the purposes of ensuring that information required to be disclosed in our SEC reports is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our CEO as appropriate to allow timely decisions regarding required disclosure.

As of the end of the period covered by this report, we have carried out an evaluation, under the supervision and with the participation of our CEO of the effectiveness of the design and operation of our disclosure controls and procedures. Based upon that evaluation, our CEO, who is also our CFO, concluded that our disclosure controls and procedures are effective for the purposes discussed above. There have been no significant changes in our internal controls or in other factors that could significantly affect these

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controls subsequent to the date of the evaluation.

PART II-OTHER INFORMATION

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits:

31 - SOX 302 Certification

32 - SOX 906 Certification

Signature

In accordance with the requirements of the Exchange Act, the Registrant has caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

HALLADOR PETROLEUM COMPANY

Dated: November 14, 2003

By: /S/VICTOR P. STABIO
Chief Executive Officer and
Chief Financial Officer

Signing on behalf of registrant
and as principal financial officer.