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HALLADOR PETROLEUM CO  
Form 10QSB  
August 16, 2004

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 June 30, 2004

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

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

303-839-5504 FAX: 303-832-3013  
(Issuer's telephone numbers)

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 August 16, 2004: 7,093,150

PART I - FINANCIAL INFORMATION

Consolidated Balance Sheet  
(in thousands)

|                           | June 30,<br>2004 | December 31,<br>2003* |
|---------------------------|------------------|-----------------------|
|                           | -----            | -----                 |
| ASSETS                    |                  |                       |
| Current assets:           |                  |                       |
| Cash and cash equivalents | \$ 4,169         | \$ 3,319              |
| Accounts receivable-      |                  |                       |
| Oil and gas sales         | 1,142            | 1,019                 |

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|  |          |          |
|--|----------|----------|
| Well operations  | 326      | 543      |
|  | -----    | -----    |
| Total current assets   | 5,637    | 4,881    |
|  | -----    | -----    |
| Oil and gas properties, at cost (successful efforts):                                    |          |          |
| Unproved properties  | 392      | 450      |
| Proved properties  | 26,185   | 25,910   |
| Less - accumulated depreciation,<br>depletion, amortization and impairment               | (20,225) | (19,749) |
|  | -----    | -----    |
|  | 6,352    | 6,611    |
|  | -----    | -----    |
| Oil and gas operator bonds   | 216      | 216      |
| California plug and abandonment deposits   | 365      | 291      |
| Investment in Catalytic Solutions  | 150      | 164      |
| Other assets   | 50       | 49       |
|  | -----    | -----    |
|  | \$12,770 | \$12,212 |
|  | =====    | =====    |
| LIABILITIES AND STOCKHOLDERS' EQUITY   |          |          |
| Current liabilities:   |          |          |
| Accounts payable and accrued liabilities   | \$ 812   | \$ 1,383 |
| Oil and gas sales payable  | 660      | 598      |
|  | -----    | -----    |
| Total current liabilities  | 1,472    | 1,981    |
|  | -----    | -----    |
| Key employee bonus plan  | 284      | 253      |
|  | -----    | -----    |
| Future site restoration  | 1,346    | 1,294    |
|  | -----    | -----    |
| Minority interest  | 5,342    | 5,047    |
|  | -----    | -----    |
| Commitments and contingencies  |          |          |
| Stockholders' equity:  |          |          |
| Preferred stock, \$.10 par value;<br>10,000,000 shares authorized; none issued           |          |          |
| Common stock, \$ .01 par value; 100,000,00<br>shares authorized, 7,093,150 shares issued | 71       | 71       |
| Additional paid-in capital   | 18,061   | 18,061   |
| Accumulated deficit  | (13,806) | (14,495) |
|  | -----    | -----    |
|  | 4,326    | 3,637    |
|  | -----    | -----    |
|  | \$12,770 | \$12,212 |
|  | =====    | =====    |

\*Derived from the Form 10-KSB.

See accompanying notes.

Consolidated Statement of Operations  
(in thousands)

| Six months ended |       | Three months ended |       |
|------------------|-------|--------------------|-------|
| June 30,         |       | June 30,           |       |
| 2004             | 2003  | 2004               | 2003  |
| -----            | ----- | -----              | ----- |

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|  |         |         |         |         |
|--|---------|---------|---------|---------|
| Revenue:   |         |         |         |         |
| Oil  | \$3,852 | \$3,828 | \$2,055 | \$1,725 |
| Gas  | 955     | 835     | 491     | 487     |
| Other  | 126     | 109     | 23      |         |
|  | -----   | -----   | -----   | -----   |
|  | 4,933   | 4,772   | 2,569   | 2,212   |
|  | -----   | -----   | -----   | -----   |
| Costs and expenses:  |         |         |         |         |
| Lease operating  | 2,691   | 2,731   | 1,569   | 1,494   |
| Exploration costs  | 140     | 145     | 110     | 125     |
| Depreciation, depletion and<br>amortization                          | 530     | 562     | 265     | 277     |
| General and administrative   | 587     | 585     | 296     | 246     |
|  | -----   | -----   | -----   | -----   |
|  | 3,948   | 4,023   | 2,240   | 2,142   |
|  | -----   | -----   | -----   | -----   |
| Income before cumulative effect of<br>change in accounting principle | 985     | 749     | 329     | 70      |
| Cumulative effect of change in<br>accounting principle               |         | (181)   |         |         |
|  | -----   | -----   | -----   | -----   |
| Income before minority interest                                      | 985     | 568     | 329     | 70      |
| Minority interest  | (296)   | (170)   | (99)    | (21)    |
|  | -----   | -----   | -----   | -----   |
| Net income   | \$ 689  | \$ 398  | \$ 230  | \$ 49   |
|  | =====   | =====   | =====   | =====   |
| Income per share   |         |         |         |         |
| Before cumulative effect of<br>change in accounting principle        | \$ .10  | \$ .07  | \$ .03  | \$ .01  |
| Cumulative effect of change<br>in accounting principle               |         | (.02)   |         |         |
|  | -----   | -----   | -----   | -----   |
| Net income   | \$ .10* | \$ .05  | \$ .03  | \$ .01  |
|  | =====   | =====   | =====   | =====   |
| Weighted average shares outstanding<br>-basic                        | 7,093   | 7,093   | 7,093   | 7,093   |
|  | =====   | =====   | =====   | =====   |

\*Diluted income per share was \$.09 and diluted weighted average shares outstanding were 7,500. Basic and diluted income per share were the same for the other periods.

See accompanying notes.

Consolidated Statement of Cash Flows  
(in thousands)

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|  | Six months ended June 30,<br>2004 | 2003    |
|--|-----------------------------------|---------|
|  | -----                             | -----   |
| Net cash provided by operating activities      | \$1,169                           | \$1,548 |
|  | -----                             | -----   |
| Cash flows from investing activities:          |                                   |         |
| Properties                                     | (245)                             | (262)   |
| Other  | (74)                              | (90)    |
|  | -----                             | -----   |
| Net cash used in investing activities          | (319)                             | (352)   |
|  | -----                             | -----   |
| Cash flows from financing activities:          |                                   |         |
| Debt retirement                                |                                   | (251)   |
| Cash calls from joint interest owners          |                                   | 351     |
|  |                                   | -----   |
| Net cash from financing activities             |                                   | 100     |
|  |                                   | -----   |
| Net increase in cash and cash equivalents      | 850                               | 1,296   |
|  |                                   | -----   |
| Cash and cash equivalents, beginning of period | 3,319                             | 1,647   |
|  | -----                             | -----   |
| Cash and cash equivalents, end of period       | \$4,169                           | \$2,943 |
|  | =====                             | =====   |

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 2003 Form 10-KSB. This quarterly report should be read in conjunction with that annual report.
3. In July 2001, the FASB issued SFAS 143, Accounting for Asset Retirement Obligations. SFAS 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 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. On October 1, 2003 we changed our estimate and increased our liability by an additional \$300,000. For the six months ended June 30, 2004 and 2003, we recognized \$52,000 and \$37,000, respectively, of accretion on the liability as a component of depletion expense.
4. As allowed in SFAS 123, Accounting for Stock-Based Compensation, we continue to apply APB 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 was not material for any

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of the periods presented. No grants were issued during the 2004 and 2003 periods.

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 Los Angeles 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.

6. On August 10, 2004, we entered into an agreement with E&B Natural Resources Management Corporation (a private company) to sell all of our interest in the South Cuyama field and adjacent exploration areas for \$23 million; consisting of \$19.5 million in cash and an interest bearing note of \$3.5 million due on September 30, 2005. Due to the minority interest these amounts will be reduced by 30%. Closing is scheduled for September 30, 2004, with an effective date of June 1, 2004.

Due to the effective date being June 1, 2004, downward closing adjustments are expected to be about \$1.5 million. In addition, and subject to final board approval, we plan to make employee bonuses and retention payments and to cash out our outstanding stock options all totaling about \$2.7 million. Currently there are about 750,000 options outstanding and after the stock option cash out these options will be canceled.

Following the sale, we will have no California operations, but will continue our operations in New Mexico and Texas. These properties have remaining gas reserves of about 2 BCF natural gas equivalents or 1.5 BCF considering the 30% minority interest.

After closing, our board will meet to consider how best to utilize the cash from the sale. Among the options the board will consider is a special dividend. We have about 7.1 million shares outstanding.

As a result of the sale agreement discussed above all exploration activities have been put on hold pending closing of the sale.

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

RESULTS OF OPERATIONS

YEAR-TO-DATE COMPARISON

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

|                     | 2004            |                  |         | 2003            |                  |         |
|---------------------|-----------------|------------------|---------|-----------------|------------------|---------|
|                     | Sales<br>Volume | Average<br>Price | Revenue | Sales<br>Volume | Average<br>Price | Revenue |
| Oil - barrels       |                 |                  |         |                 |                  |         |
| South Cuyama field  | 107             | \$35.00          | \$3,745 | 130             | \$28.82          | \$3,746 |
| Other               | 4               | 26.75            | 107     | 5               | 16.40            | 82      |
| Gas - mcf           |                 |                  |         |                 |                  |         |
| South Cuyama field  | 111             | 5.66             | 628     | 79              | 5.56             | 439     |
| San Juan-New Mexico | 35              | 4.97             | 174     | 26              | 4.57             | 119     |
| Other               | 27              | 5.67             | 153     | 45              | 6.15             | 277     |

Oil revenue stayed about the same; however, the production declines were more than offset by price increases as set forth in the table above. Field production to the 100% for the 2004 and 2003 periods averaged 800 and 958 bopd, respectively. Oil production is down due to mechanical failures on three of our better wells and the decision not to start new projects pending the sale of the field. Current field production to the 100% is about 835 bopd. Gas revenue increased primarily due to higher production in the field. Last year the gas was shut in for about 50 days due to gas quality issues with SOCAL as previously disclosed in our 2003 Form 10-KSB.

Current prices are about \$44 for oil and \$6 for gas.

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

|                           | 2004    | 2003    |
|---------------------------|---------|---------|
| South Cuyama field:       |         |         |
| LOE excluding electricity | \$2,002 | \$1,900 |
| Electricity               | 606     | 694     |
|                           | 2,608   | 2,594   |
| San Juan - New Mexico     | 63      | 78      |
| Other                     | 20      | 59      |
|                           | \$2,691 | \$2,731 |

Electricity decreased due to a 17% rate reduction from PG&E.

QUARTER-TO-DATE COMPARISON

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

|                     | 2004            |                  |         | 2003            |                  |         |
|---------------------|-----------------|------------------|---------|-----------------|------------------|---------|
|                     | Sales<br>Volume | Average<br>Price | Revenue | Sales<br>Volume | Average<br>Price | Revenue |
|                     | -----           | -----            | -----   | -----           | -----            | -----   |
| Oil - barrels       |                 |                  |         |                 |                  |         |
| South Cuyama field  | 55              | \$36.36          | \$2,000 | 64              | \$26.33          | \$1,685 |
| Other               | 2               | 27.50            | 55      | 4               | 10.00            | 40      |
| Gas - mcf           |                 |                  |         |                 |                  |         |
| South Cuyama field  | 56              | 5.77             | 323     | 58              | 5.47             | 317     |
| San Juan-New Mexico | 19              | 5.16             | 98      | 13              | 4.38             | 57      |
| Other               | 12              | 5.83             | 70      | 19              | 5.95             | 113     |

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

|                           | 2004    | 2003    |
|---------------------------|---------|---------|
|                           | -----   | -----   |
| South Cuyama field:       |         |         |
| LOE excluding electricity | \$1,235 | \$1,042 |
| Electricity               | 294     | 374     |
|                           | -----   | -----   |
|                           | 1,529   | 1,416   |
| San Juan - New Mexico     | 35      | 52      |
| Other                     | 5       | 26      |
|                           | -----   | -----   |
|                           | \$1,569 | \$1,494 |
|                           | =====   | =====   |

Field production to the 100% for the periods ended June 30, 2004 and 2003 averaged 820 and 962 bopd, respectively.

The increase in G&A was due primarily to a \$50,000 contribution to a Denver charity.

The explanations above for the year-to-date comparisons also apply to the quarter-to-date comparisons.

### LIQUIDITY AND CAPITAL RESOURCES

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

We have no bank debt, no special purpose entities and no off-balance sheet

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arrangements nor did we enter into any related party transactions.

THE FOLLOWING DISCUSSION UPDATES THE MD&A CONTAINED IN ITEM 6 OF THE 2003 FORM 10-KSB AND THE TWO DISCUSSIONS SHOULD BE READ TOGETHER.

### PROSPECT DEVELOPMENT AND EXPLORATION ACTIVITY

#### SOUTH CUYAMA FIELD

On August 10, 2004, we entered into an agreement with E&B Natural Resources Management Corporation (a private company) to sell all of our interest in the South Cuyama field and adjacent exploration areas for \$23 million; consisting of \$19.5 million in cash and an interest bearing note of \$3.5 million due on September 30, 2005. Due to the minority interest these amounts will be reduced by 30%. Closing is scheduled for September 30, 2004, with an effective date of June 1, 2004.

Due to the effective date being June 1, 2004, downward closing adjustments are expected to be about \$1.5 million. In addition, and subject to final board approval, we plan to make employee bonuses and retention payments and to cash out our outstanding stock options all totaling about \$2.7 million. Currently there are about 750,000 options outstanding and after the stock option cash out these options will be canceled.

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After closing, our board will meet to consider how best to utilize the cash from the sale. Among the options the board will consider is a special dividend. We have about 7.1 million shares outstanding.

As a result of the sale agreement discussed above all exploration activities have been put on hold pending closing of the sale.

#### SOCAL

The pipeline matter discussed in the 2003 Form 10-KSB has been favorably resolved.

There are no other significant changes or developments to report from what we disclosed in the 2003 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 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

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the purposes discussed above. There have been no significant changes in our internal controls or in other factors that could significantly affect these 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

99 -- Purchase and Sale Agreement Among Hallador Petroleum Company, Hallador Production Company, Hallador Petroleum, LLP, Santa Barbara Partners, Trio Petroleum Inc., Cuyama Drilling and Production Company and South Cuyama Limited Partnership ("Sellers") and E&B Natural Resources Management Corporation and WRBD II, LP ("Buyers") dated August 10, 2004

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: August 16, 2004

By: /s/ VICTOR P. STABIO  
CEO and CFO  
Signing on behalf of registrant  
and as principal financial officer.