HALLADOR PETROLEUM CO
Form 10QSB
August 14, 2003

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

FORM 10-QSB

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

For the quarterly period ended June 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	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 [x] No [ ]

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

PART I - FINANCIAL INFORMATION

Consolidated Balance Sheet
(in thousands)

	June 30, 2003	December 31, 2002*

ASSETS		
Current assets:		
Cash and cash equivalents	$ 2,943	$ 1,647
Accounts receivable-		
Oil and gas sales	783	680
Well operations	262	146
Total current assets	3,988	2,473
Oil and gas properties, at cost (successful efforts):		
Unproved properties	249	247
Proved properties	25,321	25,058
Less - accumulated depreciation,		
Depletion, amortization and impairment	(19,270)	(18,836)
	6,300	6,469
Oil and gas operator bonds	507	417
Investment in Catalytic Solutions	164	164
Other assets	35	38
	$10,994	$ 9,561
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable and accrued liabilities	$ 1,086	$ 527
Oil and gas sales payable	414	185
Total current liabilities	1,500	712
Bank debt		251
Key employee bonus plan	236	209
Future site restoration-South Cuyama Field	954	653
Minority interest	4,933	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	(14,761)	(15,159)
	3,371	2,973
	$10,994	$ 9,561

*Derived from the Form 10-KSB.

See accompanying notes.

Consolidated Statement of Operations
(in thousands)

	Six months ended June 30, 2003	Six months ended June 30, 2002	Three months ended June 30, 2003	Three months ended June 30, 2002
Revenue:				
Oil	$3,828	$2,881	$1,725	$1,559
Gas	835	559	487	302
Realized gain (loss) on crude oil puts	39		(18)	
Interest and other	70	25	15	17
	4,772	3,465	2,209	1,878
Costs and expenses:				
Lease operating	2,731	2,266	1,494	1,191
Exploration costs	145	47	125	28
Impairment-Fulton Fuller gas well		79		79
Impairment-S.E. Bonus Field		840		840
Depreciation, depletion and amortization	562	1,346	277	654
General and administrative	585	450	243	217
	4,023	5,028	2,139	3,009
Income (loss) before cumulative effect of change in accounting principle	749	(1,563)	70	(1,131)
Cumulative effect of change in accounting principle	(181)			
Income (loss) before minority interest	568	(1,563)	70	(1,131)
Minority interest	(170)	469	(21)	339
Net income (loss)	$ 398	$(1,094)	$ 49	$ (792)
Income (loss) per share-basic and diluted:				
Before cumulative effect of change in accounting principle	$ .07	$ (.15)	$ .01	$ (.11)
Cumulative effect of change in accounting principle	(.02)			
Net income (loss)	$ .05	$ (.15)	$ .01	$ (.11)
Weighted average shares outstanding-basic	7,093	7,093	7,093	7,093

See accompanying notes.

Consolidated Statement of Cash Flows
(in thousands)

	Six months ended June 30, 2003	2002
Net cash provided by operating activities	$1,548	$1,029
Cash flows from investing activities:		
Properties	(262)	(966)
Operator bonds	(90)	(52)
Net cash used in investing activities	(352)	(1,018)
Cash flows from financing activites:		
Debt retirement	(251)	
Cash calls from joint interest owners	351	
Net cash from financing activities	100	
Net increase in cash and cash equivalents	1,296	11
Cash and cash equivalents, beginning of period	1,647	2,078
Cash and cash equivalents, end of period	$ 2,943	$2,089

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 six months ended June 30, 2003, we recognized $37,000 of accretion on the liability as a component of depletion expense.

   Had SFAS No. 143 been adopted on January 1, 2002, the pro forma net loss would have been $1,147,000 and the pro forma net loss per share would have been $(.16) for the six months ended June 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 supplemental disclosures required by SFAS No. 123, as amended in SFAS No. 148, "Accounting for Stock-Based Compensation - Transition and Disclosure," related to our stock option plan are presented below.

   Under SFAS No. 123, compensation cost would be recognized for the fair value of the employee's option rights. The fair value of each option was estimated on the date of grant using the Black-Scholes option-pricing model with the following assumptions for option grants made in 2002 (there were no grants issued in the first six months of 2003):

	2002
Expected option life	10 years
Volatility	120%
Risk-free interest rate	4.14%

   Had compensation cost for our stock based compensation plan been based upon the fair value at the grant dates for awards under the plan consistent with the method of SFAS No. 123 using the Black-Scholes model, our net income and earnings per share would have been recorded as the pro forma amounts indicated below for the six months ended June 30, 2003 and 2002 (in thousands, except per share data):

	2003	2002
Net income (loss):		
As reported	$ 398	$(1,094)
Pro forma	373	(1,127)
Basic and diluted net income (loss) per share:		
As reported	.05	(.15)
Pro forma	.05	(.16)

5. Through mid February 2003, we had never entered into any commodity derivative agreements since acquiring the SC Field. During mid February 2003 oil prices in the field reached a level of about $36 per barrel. For the first time we purchased puts on 23,000 barrels of oil for the month of June 2003 (strike price of $29.00 per barrel) and 16,500 barrels of oil for the month of July 2003 (average strike price of $30.48 per barrel). Our total investment was $83,000. At March 31, 2003 the fair value of these puts was $140,000. During the second quarter we sold the puts for $122,000. Our net gain from this transaction was $39,000. For accounting purposes we realized a gain of $57,000 in the first quarter and in the second quarter we recognized a loss of $18,000.

6. 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	130	$28.82	$3,746	135	$20.70	$2,795
Other	5	16.40	82	6	14.33	86
Gas - mcf						
South Cuyama field	79	5.56	439	49	2.96	145
San Juan-New Mexico	26	4.57	119	26	1.92	50
Other	45	6.15	277	128	2.84	364

Oil and gas revenue increased due to higher prices as set forth in the Table above. Decrease in other gas production was due to the 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.

Current prices for the South Cuyama field are about $29.42 for oil and $5.00 for gas and San Juan gas is about $4.40.

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

	2003	2002
South Cuyama field:		
LOE excluding electricity	$1,900	$1,439
Electricity	694	696

	2,594	2,135
San Juan-New Mexico	78	30
Other	59	101
Total	$2,731	$2,266

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 CO_2 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 increase in exploration costs was due primarily to a late billing for $64,000 relating to 3-D work performed in the fourth quarter 2002.

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, higher employee costs - $32,000, higher legal fees associated with the ARCO Indemnity and SOCAL negotiations - $24,000, and other minor increases of $19,000.

DD&A decreased due to higher reserve estimates at June 30, 2003 compared to June 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	64	$26.33	$1,685	65	$23.32	$1,516
Other	4	10.00	40	3	14.33	43
Gas - mcf						
South Cuyama field	58	5.47	317	23	3.48	80
San Juan-New Mexico	13	4.38	57	13	2.38	31
Other	19	5.95	113	55	3.47	191

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

	2003	2002
South Cuyama field:		

LOE excluding electricity	$1,042	$ 752
Electricity	374	377
	1,416	1,129
San Juan-New Mexico	52	13
Other	26	49
Total	$1,494	$1,191

The explanations above for the year-to-date comparisons also apply to the quarter-to-date comparisons, other than for G&A.

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

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 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 development wells. We are still in the process of perforating and production testing. 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.

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 1,800 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. We should know in the next 30 days the results of these negotiations.

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.

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. In July and August, we drilled three more successful development gas wells. These five wells cost about $3 million to the 100%. We have an approximate 10% WI in these five 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 6%. One more development gas well is planned before the end of the year and that will conclude our development activity in this area.

Crude Oil Put Options

Through mid February 2003, we had never entered into any commodity derivative agreements since acquiring the SC Field. During mid February 2003 oil prices in the field reached a level of about $36 per barrel. For the first time we purchased puts on 23,000 barrels of oil for the month of June 2003 (strike price of $29.00 per barrel) and 16,500 barrels of oil for the month of July 2003 (average strike price of $30.48 per barrel). Our total investment was $83,000. At March 31, 2003 the fair value of these puts was $140,000. During the second quarter we sold the puts for $122,000. Our net gain from this transaction was $39,000. For accounting purposes we realized a gain of $57,000 in the first quarter and in the second quarter we recognized a loss of $18,000.

Predecessor Entity

Over the past 12 years we have paid about $200,000 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 six months ended June 30, 2003 and 2002, we have spent less than $2,000 for these type of costs. 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 six months ended June 30, 2003, we recognized $37,000 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 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

(b) Form 8-K dated June 27, 2003 - Item 4. Change in Registrant's Certifying Accountant.

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 14, 2003

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

Signing on behalf of registrant
and as principal financial officer.