

FELLOWS ENERGY LTD  
Form SB-2  
November 10, 2005

As filed with the Securities and Exchange Commission on November 10, 2005  
An Exhibit List can be found on page II-5.  
Registration No. 333-

UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON D.C. 20549

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FORM SB-2  
REGISTRATION STATEMENT  
UNDER  
THE SECURITIES ACT OF 1933

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**FELLOWS ENERGY LTD.**

(Name of small business issuer in its charter)

**Nevada**  
(State or other Jurisdiction  
of Incorporation or Organization)

**1382**  
(Primary Standard Industrial  
Classification Code Number)

**33-0967648**  
(I.R.S. Employer  
Identification No.)

**370 Interlocken Boulevard, Suite 400  
Broomfield, Colorado 80021  
(303) 327-1525**

(Address and telephone number of principal executive offices and principal place of business)

**George S. Young, Chief Executive Officer  
FELLOWS ENERGY LTD.  
370 Interlocken Boulevard, Suite 400  
Broomfield, Colorado 80021  
(303) 327-1525**

(Name, address and telephone number of agent for service)

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**APPROXIMATE DATE OF PROPOSED SALE TO THE PUBLIC:**

From time to time after this Registration Statement becomes effective.

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If any securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, other than securities offered only in connection with dividend or interest reinvestment plans, check the following box:

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If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. [ ] \_\_\_\_\_

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. [ ] \_\_\_\_\_

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. [ ] \_\_\_\_\_

If delivery of the prospectus is expected to be made pursuant to Rule 434, please check the following box. [ ] \_\_\_\_\_

**CALCULATION OF REGISTRATION FEE**

| <b>Title of each class of securities to be registered</b>                         | <b>Amount to be registered (1)</b> | <b>Proposed maximum offering price per share (2)</b> | <b>Proposed maximum aggregate offering price</b> | <b>Amount of registration fee</b> |
|---|------------------------------------|--|--|-----------------------------------|
| Common stock, \$.001 par value issuable upon conversion of Convertible Debentures | 7,770,000 (3)                      | \$0.53   | \$4,118,100                                      | \$484.70                          |
| Common Stock, \$.001 par value issuable upon exercise of Warrants                 | 2,823,600 (4)                      | \$0.80   | \$2,258,880                                      | \$265.87                          |
| <b>Total</b>  | <b>10,593,600</b>                  |  | <b>\$6,376,980</b>                               | <b>\$750.57</b>                   |

(1) Includes shares of our common stock, par value \$0.001 per share, which may be offered pursuant to this registration statement, which shares are issuable upon conversion of convertible debentures and the exercise of warrants held by the selling stockholders. In addition to the shares set forth in the table, the amount to be registered includes an indeterminate number of shares issuable upon conversion of the convertible debentures and exercise of the warrants, as such number may be adjusted as a result of stock splits, stock dividends and similar transactions in accordance with Rule 416. The number of shares of common stock registered hereunder represents a good faith estimate by us of the number of shares of common stock issuable upon conversion of the convertible debentures and upon exercise of the warrants. For purposes of estimating the number of shares of common stock to be included in this registration statement, we calculated a good faith estimate of the number of shares of our common stock that we believe will be issuable upon conversion of the convertible debentures and upon exercise of the warrants to account for market fluctuations, and antidilution and price protection adjustments, respectively. Should the conversion ratio result in our having insufficient shares, we will not rely upon Rule 416, but will file a new registration statement to cover the resale of such additional shares should that become necessary. In addition, should a decrease in the exercise price as a result of an issuance or sale of shares below the then current market price, result in our having insufficient shares, we will not rely upon Rule 416, but will file a new registration statement to cover the resale of such additional shares should that become necessary.

(2) Estimated solely for purposes of calculating the registration fee in accordance with Rule 457(c) and Rule 457(g) under the Securities Act of 1933, using the average of the high and low price as reported on the Over-The-Counter Bulletin Board on November 9, 2005, which was \$.53 per share.

(3) Includes a good faith estimate of the shares underlying convertible debentures to account for market fluctuations.

(4) Includes a good faith estimate of the shares underlying warrants exercisable at \$.80 per share to account for antidilution and price protection adjustments.

**The registrant hereby amends this registration statement on such date or dates as may be necessary to delay its effective date until the registrant shall file a further amendment which specifically states that this registration statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933 or until the registration statement shall become effective on such date as the Commission, acting pursuant to said Section 8(a), may determine.**

**Preliminary Prospectus**

SUBJECT TO COMPLETION, DATED NOVEMBER 10, 2005

**The information in this preliminary prospectus is not complete and may be changed. The securities being registered by the Registration Statement may not be sold until the Registration Statement filed with the Securities and Exchange Commission is effective. This prospectus is neither an offer to sell these securities nor a solicitation of an offer to buy these securities in any state where the offer or sale is not permitted.**

**FELLOWS ENERGY LTD.**

**10,593,600 Shares of Common Stock**

This prospectus relates to the resale by the selling stockholders of up to 10,593,600 shares of our common stock, including up to 7,770,000 shares of common stock underlying convertible debentures in a principal face amount of \$3,108,000 and up to 2,823,600 shares of common stock issuable upon the exercise of common stock purchase warrants. The convertible debentures are unsecured and we are obligated to pay 1/24th of the face amount of the convertible debentures on the first of every month, starting January 1, 2006, which payment can be made in cash or in our restricted common stock. We may pay this amortization payment in cash or in stock at the lower of (i) \$0.75 per share or (ii) 80% of the volume weighted average price of our stock for the five trading days prior to the repayment date. In the event that we make the payment in cash, we shall pay 110% of the monthly redemption amount. Except as provided herein and to the extent any debentures remain outstanding, at any time, the debentures are convertible into shares of our common stock at \$0.75 per share. The selling stockholders may sell common stock from time to time in the principal market on which the stock is traded at the prevailing market price or in negotiated transactions. The selling stockholders may be deemed underwriters of the shares of common stock, which they are offering. We will pay the expenses of registering these shares.

HPC Capital Management, a registered broker-dealer, who received its shares of common stock being offering in this prospectus as compensation for investment banking services and holds the securities for its own account, may be deemed an underwriter within the meaning of the Securities Act of 1933 in connection with the sale of its common stock under this prospectus. With the exception of the above listed entity, no other underwriter or person has been engaged to facilitate the sale of shares of common stock in this offering.

Our common stock is registered under Section 12(g) of the Securities Exchange Act of 1934 and is traded on the Over-The-Counter Bulletin Board under the symbol "FLWE". The last reported sales price per share of our common stock as reported by the Over-The-Counter Bulletin Board on November 9, 2005, was \$.55.

**Investing in these securities involves significant risks. See "Risk Factors" beginning on page 8.**

**Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this Prospectus is truthful or complete. Any representation to the contrary is a criminal offense.**

The date of this prospectus is \_\_\_\_\_, 2005.



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**You should rely only on the information contained in this prospectus. We have not authorized any person to provide you with different information. If anyone provides you with different information, you should not rely on it. You should assume that the information appearing in this prospectus is accurate only as of the date on the front cover of this prospectus.**

**CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS**

This prospectus and any prospectus supplement contain forward-looking statements. We have based these forward-looking statements on our current expectations and projections about future events.

In some cases you can identify forward-looking statements by words such as "may," "should," "expect," "plan," "could," "anticipate," "intend," "believe," "estimate," "predict," "potential," "goal," or "continue" or similar terminology. These statements are only predictions and involve known and unknown risks, uncertainties and other factors, including the risks outlined under "Risk Factors," that may cause our or our industry's actual results, levels of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed or implied by such forward-looking statements.

Unless we are required to do so under U.S. federal securities laws or other applicable laws, we do not intend to update or revise any forward-looking statements.



## PROSPECTUS SUMMARY

The following summary highlights selected information contained in this prospectus. This summary does not contain all the information you should consider before investing in the securities. Before making an investment decision, you should read the entire prospectus carefully, including the "risk factors" section, the financial statements and the notes to the financial statements.

### FELLOWS ENERGY LTD.

We are an early stage oil and gas company led by an experienced management team and focused on exploration and production of natural gas, especially from "unconventional plays" such as tight sands and coal beds, and oil in the Rocky Mountain Region. In many unconventional plays accumulations of hydrocarbons are found over a large areal expanse and/or a thick vertical section, which when compared to conventional plays, typically have a higher geological and/or commercial development risk and lower average decline rate. Whereas a "conventional play" is an accumulation of hydrocarbons in a structural or stratigraphic setting within high-quality reservoirs. Our strategy is to pursue selected opportunities that are characterized by reasonable entry costs, favorable economic terms, high reserve potential relative to capital expenditures and the availability of existing technical data that may be further developed using current technology.

On January 5, 2004, we acquired certain interests in certain oil and gas leases and other interests owned by Diamond Oil & Gas Corporation, a Nevada corporation. Diamond is wholly owned by George S. Young, CEO, President and a Director of Fellows.

In connection with the transaction with Diamond, we (1) issued 3,500,000 shares of our common stock to Diamond; (ii) completed a private placement of \$2,750,000, pursuant to which we issued 2,750,000 shares of our common stock at \$1.00 per share; (3) appointed George S. Young as our President, Chief Executive Officer and a Director and Steven L. Prince as our Vice President and a Director; and (4) accepted the resignation of our then management and redeemed 52,610,000 shares of our common stock owned by the outgoing and former management in exchange for an aggregate sum of \$27,000.

For the years ended December 31, 2004 and 2003, we did not generate any revenues and had net losses of \$3,760,308 and \$123,475, respectively. For the six months ended June 30, 2005, we did not generate any revenues and had net income of \$713,430 as a result of a gain on the sale of property of \$1,437,281. As a result of significant losses from operations, our Independent Registered Public Accounting Firm, in their report dated March 29, 2005, have expressed substantial doubt about our ability to continue as going concern.

Our principal offices are located at 370 Interlocken Boulevard, Suite 400 Broomfield, Colorado 80021, and our telephone number is (303) 327-1525. We are a Nevada corporation.

### The Offering

Common stock offered by selling  
stockholders.....

Up to 10,593,600 shares, including the following:

- up to 7,770,000 shares of common stock underlying convertible debentures in the principal amount of \$3,108,000 (includes a good faith estimate of the shares underlying convertible debentures to account for

market fluctuations and antidilution protection adjustments,  
respectively), and

- up to 2,823,600 shares of common stock issuable upon the exercise of common stock purchase warrants at an exercise price of \$.80 per share (includes a good faith estimate of the shares underlying warrants to account for antidilution protection adjustments).

Common stock to be outstanding after the offering.....

Up to 58,472,406 shares

U s e o  
proceeds.....

fWe will not receive any proceeds from the sale of the common stock. However, we will receive the sale price of any common stock we sell to the selling stockholders upon exercise of the warrants. We expect to use the proceeds received from the exercise of the warrants, if any, for general working capital purposes. However, Palisades Master Fund, L.P. and Crescent International Ltd. will be entitled to exercise up to 2,693,600 warrants on a cashless basis if the shares of common stock underlying the warrants are not registered pursuant to an effective registration statement at any time after one year from issuance. In the event that Palisades Master Fund, L.P. or Crescent International Ltd. exercise the warrants on a cashless basis, then we will not receive any proceeds from the exercise of those warrants.

Over-The-Counter Bulletin Board  
Symbol.....

FLWE

The above information regarding common stock to be outstanding after the offering is based on 47,878,806 shares of common stock outstanding as of October 21, 2005 and assumes the subsequent conversion of our issued convertible debentures and exercise of warrants by our selling stockholders.

**September 2005 Private Placement**

On September 21, 2005, we closed a financing pursuant to a securities purchase agreement with two accredited investors for the issuance of \$3,108,000 in face amount of debentures maturing December 21, 2008, and three year warrants to purchase our common stock. The debentures do not accrue interest and the investors paid \$2,174,947.52 for the debentures. A commission of 8% on \$2,000,000 was paid by us to HPC Capital Management, a registered broker-dealer, in connection with the transaction, and we placed \$50,000 in escrow for the payment of future legal fees, resulting in net proceeds to us of \$1,964,947.52 before our legal fees. Net proceeds will be used by us for general working capital.

The debentures are unsecured and we are obligated to pay 1/24th of the face amount of the debenture on the first of every month, starting January 1, 2006, which payment can be made in cash or in shares of our common stock. We may pay this amortization payment in cash or in stock at the lower of \$0.75 per share or 80% of the volume weighted average price of our stock for the five trading days prior to the repayment date. In the event that we make the payment in cash, we shall pay 110% of the monthly redemption amount.

Except as provided in the succeeding paragraph and to the extent any debentures remain outstanding, at any time, the debentures are convertible into shares of our common stock at \$0.75 per share.

At any time after 90 days from the date that a registration statement registering the shares of common stock underlying the debentures and warrants is declared effective, and if certain conditions are met, we have the right to redeem some or all of the debentures in a cash amount equal to 110% of the face amount of the debentures being redeemed.

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After the registration statement registering the shares of common stock underlying the debentures and warrants is declared effective, if the closing price for our common stock exceeds \$1.875 for 20 consecutive trading days, we can require the holders to convert some or all of the debentures at \$0.75.

In the event of default, the investors may require payment, which shall be the greater of: (A) 130% of the principal amount of the face amount of the debenture to be prepaid, or (B) the principal amount of the debenture to be prepaid, divided by the conversion price on (x) the date the default amount is demanded or otherwise due or (y) the date the default amount is paid in full, whichever is less, multiplied by the closing price on (x) the date the default amount is demanded or otherwise due or (y) the date the default amount is paid in full, whichever is greater

We issued warrants to the investors, expiring September 21, 2008, to purchase 2,072,000 shares of restricted common stock, exercisable at a per share of \$0.80. In addition, the exercise price of the warrants will be adjusted in the event we issue common stock at a price below the exercise price, with the exception of any securities issued pursuant to a stock or option plan adopted by our board of directors, issued in connection with the debentures issued pursuant to the securities purchase agreement, or securities issued in connection with acquisitions or strategic transactions. Upon an issuance of shares of common stock below the exercise price, the exercise price of the warrants will be reduced to equal the share price at which the additional securities were issued and the number of warrant shares issuable will be increased such that the aggregate exercise price payable for the warrants, after taking into account the decrease in the exercise price, shall be equal to the aggregate exercise price prior to such adjustment.

Warrants to purchase 100,000 shares, at the same price and for the same term as the warrants issued to the investors, have been issued to HPC Capital Management as additional compensation for its services in connection with the transaction with the investors.

After the effective date of this registration statement, if in any period of 20 consecutive trading days our stock price exceeds 250% of the warrants' exercise price, all of the warrants shall expire on the 30th trading day after we send a call notice to the warrant holders. If at any time after one year from the date of issuance of the warrants there is not an effective registration statement registering, or no current prospectus available for, the resale of the shares underlying the warrants, then the holder may exercise the warrant at such time by means of a cashless exercise. In the event the investors exercise the warrants on a cashless basis, then we will not receive any proceeds.

The conversion price of the debentures and the exercise price of the warrants may be adjusted in certain circumstances such as if we pay a stock dividend, subdivide or combine outstanding shares of common stock into a greater or lesser number of shares, or take such other actions as would otherwise result in dilution of the investors' position.

The investors have agreed to restrict their ability to convert their debentures or exercise their warrants and receive shares of our common stock such that the number of shares of common stock held by them in the aggregate and their affiliates after such conversion or exercise does not exceed 4.99% of the then issued and outstanding shares of common stock

We agreed to file a registration statement with the Securities and Exchange Commission within 30 days of the effectiveness of the registration statement filed on August 10, 2005 (file no. 333-127413), which was declared effective on October 17, 2005, to cover the future sale by the investors of the shares issuable in payment and/or conversion of the debentures, and the shares issuable on exercise of the warrants. If the registration statement is not filed within such 30 day period or if the registration statement is not declared effective within 120 days from the date of filing, we are required to pay liquidated damages to the investors. The registration statement also will cover the future sale by HPC Capital Management of the shares issuable on exercise of the warrants issued to HPC Capital Management in connection with the transaction.



## **RISK FACTORS**

This investment has a high degree of risk. Before you invest you should carefully consider the risks and uncertainties described below and the other information in this prospectus. If any of the following risks actually occur, our business, operating results and financial condition could be harmed and the value of our stock could go down. This means you could lose all or a part of your investment.

### **Risks Relating to Our Business:**

#### **We Have a History Of Losses Which May Continue, and May Negatively Impact Our Ability to Achieve Our Business Objectives.**

We incurred net losses of \$3,760,308 and \$123,475 for the years ended December 31, 2004 and 2003, respectively. For the six months ended June 30, 2005, we achieved net income of \$472,078, which was a result of gains of approximately \$1.4 million on the sale of property. We cannot assure you that we can achieve or sustain profitability on a quarterly or annual basis in the future. Our operations are subject to the risks and competition inherent in the establishment of a business enterprise. There can be no assurance that future operations will be profitable. Revenues and profits, if any, will depend upon various factors, including whether we will be able to continue expansion of our revenue. We may not achieve our business objectives and the failure to achieve such goals would have an adverse impact on us.

#### **If We Are Unable to Obtain Additional Funding, Our Business Operations Will be Harmed and If We Do Obtain Additional Financing, Our Then Existing Shareholders May Suffer Substantial Dilution.**

We will require additional funds to sustain and expand our acquisition, exploration and production of natural gas from coal bed methane. We anticipate that we will require up to approximately \$500,000 to fund our continued operations for the next twelve months from the date of this prospectus, depending on revenues from operations. Additional capital will be required to effectively support the operations and to otherwise implement our overall business strategy. There can be no assurance that financing will be available in amounts or on terms acceptable to us, if at all. The inability to obtain additional capital will restrict our ability to grow and may reduce our ability to continue to conduct business operations. If we are unable to obtain additional financing, we will likely be required to curtail our marketing and development plans and possibly cease our operations. Any additional equity financing may involve substantial dilution to our then existing shareholders.

#### **Our Independent Registered Public Accounting Firm Has Stated There is Substantial Doubt About Our Ability to Continue As a Going Concern, Which May Hinder Our Ability to Obtain Future Financing.**

In their report dated March 29, 2005 on our financial statements as of and for the year ended December 31, 2004, our independent registered public accounting firm stated that our significant losses from operations as of September 30, 2004 raised substantial doubt about our ability to continue as a going concern. Since December 31, 2004, we have continued to experience losses from operations. Our ability to continue as a going concern is subject to our ability to generate a profit and/or obtain necessary funding from outside sources, including obtaining additional funding from the sale of our securities, increasing sales or obtaining loans and grants from various financial institutions where possible. Our continued net operating losses and stockholders' deficiency increase the difficulty in meeting such goals and there can be no assurances that such methods will prove successful.

#### **We Have a Limited Operating History and if We are not Successful in Continuing to Grow Our Business, Then We may have to Scale Back or Even Cease Our Ongoing Business Operations.**

We have no history of revenues from operations and have no significant tangible assets. We have yet to generate positive earnings and there can be no assurance that we will ever operate profitably. Our company has a limited operating history and must be considered in the development stage. Our success is significantly dependent on a successful acquisition, drilling, completion and production program. Our operations will be subject to all the risks inherent in the establishment of a developing enterprise and the uncertainties arising from the absence of a significant operating history. We may be unable to locate recoverable reserves or operate on a profitable basis. We are in the development stage and potential investors should be aware of the difficulties normally encountered by enterprises in the development stage. If our business plan is not successful, and we are not able to operate profitably, investors may lose some or all of their investment in our company.

**If We Are Unable to Retain the Services of Mr. Young or If We Are Unable to Successfully Recruit Qualified Managerial and Field Personnel Having Experience in Oil and Gas Exploration, We May Not Be Able to Continue Our Operations.**

Our success depends to a significant extent upon the continued service of Mr. George S. Young, our President, Chief Executive Officer and a director. Loss of the services of Mr. Young could have a material adverse effect on our growth, revenues, and prospective business. We do not maintain key-man insurance on the life of Mr. Young. In addition, in order to successfully implement and manage our business plan, we will be dependent upon, among other things, successfully recruiting qualified managerial and field personnel having experience in the oil and gas exploration business. Competition for qualified individuals is intense. There can be no assurance that we will be able to find, attract and retain existing employees or that we will be able to find, attract and retain qualified personnel on acceptable terms.

**As Our Properties are in the Exploration and Development Stage, There Can be no Assurance That We Will Establish Commercial Discoveries on Our Properties.**

Exploration for economic reserves of oil and gas is subject to a number of risk factors. Few properties that are explored are ultimately developed into producing oil and/or gas wells. Our properties are in the exploration and development stage only and are without proven reserves of oil and gas. We may not establish commercial discoveries on any of our properties.

**The Potential Profitability of Oil and Gas Ventures Depends Upon Factors Beyond the Control of Our Company.**

The potential profitability of oil and gas properties is dependent upon many factors beyond our control. For instance, world prices and markets for oil and gas are unpredictable, highly volatile, potentially subject to governmental fixing, pegging, controls, or any combination of these and other factors, and respond to changes in domestic, international, political, social, and economic environments. Additionally, due to worldwide economic uncertainty, the availability and cost of funds for production and other expenses have become increasingly difficult, if not impossible, to project. In addition, adverse weather conditions can also hinder drilling operations. These changes and events may materially affect our financial performance. These factors cannot be accurately predicted and the combination of these factors may result in our company not receiving an adequate return on invested capital.

**Even if We are Able to Discover and Generate A Gas Well, There Can be no Assurance the Well Will Become Profitable**

We have not yet make a discovery of coalbed methane gas or drilled a gas well to capture any gas. Even if we are able to, a productive well may become uneconomic in the event water or other deleterious substances are encountered which impair or prevent the production of oil and/or gas from the well. In addition, production from any well may be unmarketable if it is impregnated with water or other deleterious substances. In addition, the marketability of oil and



gas which may be acquired or discovered will be affected by numerous factors, including the proximity and capacity of oil and gas pipelines and processing equipment, market fluctuations of prices, taxes, royalties, land tenure, allowable production and environmental protection, all of which could result in greater expenses than revenue generated by the well.

**Competition In The Oil And Gas Industry Is Highly Competitive And There Is No Assurance That We Will Be Successful In Acquiring The Leases.**

The oil and gas industry is intensely competitive. We compete with numerous individuals and companies, including many major oil and gas companies, which have substantially greater technical, financial and operational resources and staffs. Accordingly, there is a high degree of competition for desirable oil and gas leases, suitable properties for drilling operations and necessary drilling equipment, as well as for access to funds. We cannot predict if the necessary funds can be raised or that any projected work will be completed. Our budget anticipates our acquisition of additional acreage in the Rocky Mountain Region. This acreage may not become available or if it is available for leasing, that we may not be successful in acquiring the leases.

**The Marketability of Natural Resources Will be Affected by Numerous Factors Beyond Our Control Which May Result in Us not Receiving an Adequate Return on Invested Capital to be Profitable or Viable.**

The marketability of natural resources which may be acquired or discovered by us will be affected by numerous factors beyond our control. These factors include market fluctuations in oil and gas pricing and demand, the proximity and capacity of natural resource markets and processing equipment, governmental regulations, land tenure, land use, regulation concerning the importing and exporting of oil and gas and environmental protection regulations. The exact effect of these factors cannot be accurately predicted, but the combination of these factors may result in us not receiving an adequate return on invested capital to be profitable or viable.

**Oil and Gas Operations are Subject to Comprehensive Regulation Which May Cause Substantial Delays or Require Capital Outlays in Excess of Those Anticipated Causing an Adverse Effect on Our Company.**

Oil and gas operations are subject to federal, state, and local laws relating to the protection of the environment, including laws regulating removal of natural resources from the ground and the discharge of materials into the environment. Oil and gas operations are also subject to federal, state, and local laws and regulations which seek to maintain health and safety standards by regulating the design and use of drilling methods and equipment. Various permits from government bodies are required for drilling operations to be conducted; no assurance can be given that such permits will be received. Environmental standards imposed by federal, provincial, or local authorities may be changed and any such changes may have material adverse effects on our activities. Moreover, compliance with such laws may cause substantial delays or require capital outlays in excess of those anticipated, thus causing an adverse effect on us. Additionally, we may be subject to liability for pollution or other environmental damages. To date we have not been required to spend any material amount on compliance with environmental regulations. However, we may be required to do so in future and this may affect our ability to expand or maintain our operations.

**Exploration and Production Activities are Subject to Certain Environmental Regulations Which May Prevent or Delay the Commencement or Continuance of Our Operations.**

In general, our exploration and production activities are subject to certain federal, state and local laws and regulations relating to environmental quality and pollution control. Such laws and regulations increase the costs of these activities and may prevent or delay the commencement or continuance of a given operation. Compliance with these laws and regulations has not had a material effect on our operations or financial condition to date. Specifically, we are subject to legislation regarding emissions into the environment, water discharges and storage and disposition of hazardous wastes. In addition, legislation has been enacted which requires well and facility sites to be abandoned and reclaimed to the satisfaction of state authorities. However, such laws and regulations are frequently changed and we are unable to predict the ultimate cost of compliance. Generally, environmental requirements do not appear to affect us any differently or to any greater or lesser extent than other companies in the industry.

We believe that our operations comply, in all material respects, with all applicable environmental regulations.

Our operating partners maintain insurance coverage customary to the industry; however, we are not fully insured against all possible environmental risks.

**Exploratory Drilling Involves Many Risks and We May Become Liable for Pollution or Other Liabilities Which May Have an Adverse Effect on Our Financial Position.**

Drilling operations generally involve a high degree of risk. Hazards such as unusual or unexpected geological formations, power outages, labor disruptions, blow-outs, sour gas leakage, fire, inability to obtain suitable or adequate machinery, equipment or labor, and other risks are involved. We may become subject to liability for pollution or

hazards against which it cannot adequately insure or which it may elect not to insure. Incurring any such liability may have a material adverse effect on our financial position and operations.

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**Risks Relating to Our Current Financing Arrangements:****There Are a Large Number of Shares Underlying Our Convertible Debentures and Warrants That May be Available for Future Sale and the Sale of These Shares May Depress the Market Price of Our Common Stock.**

As of October 21, 2005, we had 47,878,806 shares of common stock issued and outstanding, convertible debentures issued in June 2005 outstanding that may be converted into an estimated 10,579,231 shares of common stock at current market prices convertible debentures issued in September 2005 outstanding that may be converted into 5,976,924 shares of common stock, outstanding warrants issued in June 2005 to purchase 7,191,018 shares of common stock and outstanding warrants issued in September 2005 to purchase 2,172,000 shares of common stock. In addition, the number of shares of common stock issuable upon conversion of the outstanding convertible debentures issued in June and September 2005 may increase if the market price of our stock declines. All of the shares, including all of the shares issuable upon conversion of the June and September 2005 debentures and upon exercise of our June and September 2005 warrants, may be sold without restriction. The sale of these shares may adversely affect the market price of our common stock.

**The Continuously Adjustable Conversion Price Feature of Our Convertible Debentures Issued in September 2005 Could Require Us to Issue a Substantially Greater Number of Shares, Which Will Cause Dilution to Our Existing Stockholders.**

Our obligation to issue shares upon conversion of our convertible debentures issued in September 2005 is potentially limitless. We are required to repay 1/24th of the face amount of the debenture each month starting January 2006. In the event that we cannot, or choose not to, repay the amortized amount in cash, we are obligated to issue shares of our common stock to cover the amount of the debenture. The following is an example of the amount of shares of our common stock that are issuable, upon conversion of our convertible debentures issued in September 2005 based on market prices 25%, 50% and 75% below the market price as of November 7, 2005 of \$0.54 per share.

| <u>% Below Market</u> | <u>Price Per Share</u> | <u>With Discount at 20%</u> | <u>Number of Shares Issuable</u> | <u>% of Outstanding Stock</u> |
|-----------------------|------------------------|-----------------------------|----------------------------------|-------------------------------|
| 25%                   | \$.405                 | \$.324                      | 9,592,593                        | 16.69%                        |
| 50%                   | \$.27                  | \$.216                      | 14,388,889                       | 23.11%                        |
| 75%                   | \$.135                 | \$.108                      | 28,777,778                       | 37.54%                        |

As illustrated, the number of shares of common stock issuable upon conversion of our convertible debentures issued in September 2005 will increase if the market price of our stock declines, which will cause dilution to our existing stockholders.

**The Continuously Adjustable Conversion Price Feature of our Convertible Debentures Issued in September 2005 May Encourage Investors to Make Short Sales in Our Common Stock, Which Could Have a Depressive Effect on the Price of Our Common Stock.**

The convertible debentures issued in September 2005 are convertible into shares of our common stock at a 20% discount to the trading price of the common stock prior to the conversion. The significant downward pressure on the price of the common stock as the selling stockholders convert and sells material amounts of common stock could encourage short sales by investors. This could place further downward pressure on the price of the common stock. The selling stockholders could sell common stock into the market in anticipation of covering the short sale by converting

their securities, which could cause the further downward pressure on the stock price. In addition, not only the sale of shares issued upon conversion or exercise of convertible debentures and warrants issued in September 2005, but also the mere perception that these sales could occur, may adversely affect the market price of the common stock.

**The Issuance of Shares Upon Conversion of the Convertible Debentures Issued in September 2005 and Exercise of Outstanding Warrants May Cause Immediate and Substantial Dilution to Our Existing Stockholders.**

The issuance of shares upon conversion of the convertible debentures and exercise of warrants issued in September 2005 may result in substantial dilution to the interests of other stockholders since the selling stockholders may ultimately convert and sell the full amount issuable on conversion. Although the selling stockholders may not convert their convertible debentures and/or exercise their warrants issued in September 2005 if such conversion or exercise would cause them to own more than 4.99% of our outstanding common stock, this restriction does not prevent the selling stockholders from converting and/or exercising some of their holdings and then converting the rest of their holdings. In this way, the selling stockholders could sell more than this limit while never holding more than this limit. There is no upper limit on the number of shares that may be issued which will have the effect of further diluting the proportionate equity interest and voting power of holders of our common stock, including investors in this offering.

**In The Event That Our Stock Price Declines, The Shares Of Common Stock Allocated For Conversion Of The Convertible Debentures Issued in September 2005 and Registered Pursuant To This Prospectus May Not Be Adequate And We May Be Required to File A Subsequent Registration Statement Covering Additional Shares. If The Shares We Have Allocated And Are Registering Herewith Are Not Adequate And We Are Required To File An Additional Registration Statement, We May Incur Substantial Costs In Connection Therewith.**

Based on our current market price and the potential decrease in our market price as a result of the issuance of shares upon conversion of the convertible debentures issued in September 2005, we have made a good faith estimate as to the amount of shares of common stock that we are required to register and allocate for conversion of the convertible debentures. Accordingly, we have allocated and registered 7,770,000 shares to cover the conversion of the convertible debentures issued in September 2005. In the event that our stock price decreases, the shares of common stock we have allocated for conversion of the convertible debentures issued in September 2005 and are registering hereunder may not be adequate. If the shares we have allocated to the registration statement are not adequate and we are required to file an additional registration statement, we may incur substantial costs in connection with the preparation and filing of such registration statement.

**If We Are Required for any Reason to Repay Our Outstanding Convertible Debentures, We Would Be Required to Deplete Our Working Capital, If Available, Or Raise Additional Funds. Our Failure to Repay the Convertible Debentures, If Required, Could Result in Legal Action Against Us, Which Could Require the Sale of Substantial Assets.**

In June 2005, we entered into a Securities Purchase Agreement for the sale of an aggregate of \$5,501,199.95 principal amount of convertible debentures. The convertible debentures are due and payable 27 months from the date of issuance, with 1/24th of the face amount due every month starting October 2005. In September, 2005, we entered into a Securities Purchase Agreement for the sale of an aggregate of \$3,108,000 principal amount of convertible debentures. The convertible debentures are due and payable 27 months from the date of issuance with 1/24th of the face amount due every month starting January 2006. In addition, any event of default such as our failure to repay the principal when due, our failure to issue shares of common stock upon conversion by the holder, our failure to timely file a registration statement or have such registration statement declared effective, breach of any covenant, representation or warranty in the Securities Purchase Agreement or related convertible debentures, the assignment or appointment of a receiver to control a substantial part of our property or business, the filing of a money judgment, writ or similar process against our company in excess of \$50,000, the commencement of a bankruptcy, insolvency, reorganization or liquidation proceeding against our company and the delisting of our common stock could require the early repayment of the convertible debentures, including default interest on the outstanding principal balance of the convertible debentures if the default is not cured with the specified grace period. We anticipate that the full amount of the convertible debentures will be converted into shares of our common stock, in accordance with the terms of the convertible debentures. If we are required to repay the convertible debentures, we would be required to use our limited

working capital and raise additional funds. If we were unable to repay the convertible debentures when required, the debenture holders could commence legal action against us and foreclose on all of our assets to recover the amounts due. Any such action would require us to curtail or cease operations.

**Risks Relating to Our Common Stock:**

**If We Fail to Remain Current on Our Reporting Requirements, We Could be Removed From the OTC Bulletin Board Which Would Limit the Ability of Broker-Dealers to Sell Our Securities and the Ability of Stockholders to Sell Their Securities in the Secondary Market.**

Companies trading on the OTC Bulletin Board, such as us, must be reporting issuers under Section 12 of the Securities Exchange Act of 1934, as amended, and must be current in their reports under Section 13, in order to maintain price quotation privileges on the OTC Bulletin Board. If we fail to remain current on our reporting requirements, we could be removed from the OTC Bulletin Board. As a result, the market liquidity for our securities could be severely adversely affected by limiting the ability of broker-dealers to sell our securities and the ability of stockholders to sell their securities in the secondary market.

**Our Common Stock is Subject to the "Penny Stock" Rules of the SEC and the Trading Market in Our Securities is Limited, Which Makes Transactions in Our Stock Cumbersome and May Reduce the Value of an Investment in Our Stock.**

The Securities and Exchange Commission has adopted Rule 15g-9 which establishes the definition of a "penny stock," for the purposes relevant to us, as any equity security that has a market price of less than \$5.00 per share or with an exercise price of less than \$5.00 per share, subject to certain exceptions. For any transaction involving a penny stock, unless exempt, the rules require:

- that a broker or dealer approve a person's account for transactions in penny stocks;
- and
- that broker or dealer receive from the investor a written agreement to the transaction, setting forth the identity and quantity of the penny stock to be purchased.

In order to approve a person's account for transactions in penny stocks, the broker or dealer must:

- obtain financial information and investment experience objectives of the person;
- and
- make a reasonable determination that the transactions in penny stocks are suitable for that person and the person has sufficient knowledge and experience in financial matters to be capable of evaluating the risks of transactions in penny stocks.

The broker or dealer must also deliver, prior to any transaction in a penny stock, a disclosure schedule prescribed by the Commission relating to the penny stock market, which, in highlight form:

- sets forth the basis on which the broker or dealer made the suitability determination; and
- that the broker or dealer received a signed, written agreement from the investor prior to the transaction.

Generally, brokers may be less willing to execute transactions in securities subject to the "penny stock" rules. This may make it more difficult for investors to dispose of our common stock and cause a decline in the market value of our stock.



Disclosure also has to be made about the risks of investing in penny stocks in both public offerings and in secondary trading and about the commissions payable to both the broker-dealer and the registered representative, current quotations for the securities and the rights and remedies available to an investor in cases of fraud in penny stock transactions. Finally, monthly statements have to be sent disclosing recent price information for the penny stock held in the account and information on the limited market in penny stocks.

## USE OF PROCEEDS

We will not receive any proceeds from the sale of the common stock. However, we will receive the sale price of any common stock we sell to the selling stockholders upon exercise of the warrants. We expect to use the proceeds received from the exercise of the warrants, if any, for general working capital purposes. However, JGB Capital L.P., Palisades Master Fund, L.P. and Crescent International Ltd. will be entitled to exercise up to 2,072,000 warrants on a cashless basis if the shares of common stock underlying the warrants are not registered pursuant to an effective registration statement at any time after one year from issuance. In the event that Palisades Master Fund, L.P. or Crescent International Ltd. exercise the warrants on a cashless basis, then we will not receive any proceeds from the exercise of those warrants.

### September 2005 Private Placement

On September 21, 2005, we closed a financing pursuant to a securities purchase agreement with two accredited investors for the issuance of \$3,108,000 in face amount of debentures maturing December 21, 2008, and three year warrants to purchase our common stock. The debentures do not accrue interest and the investors paid \$2,174,947.52 for the debentures. A commission of 8% on \$2,000,000 was paid by us to HPC Capital Management, a registered broker-dealer, in connection with the transaction, and we placed \$50,000 in escrow for the payment of future legal fees, resulting in net proceeds to us of \$1,964,947.52 before our legal fees. Net proceeds will be used by us for general working capital.

The debentures are unsecured and we are obligated to pay 1/24th of the face amount of the debenture on the first of every month, starting January 1, 2006, which payment can be made in cash or in shares of our common stock. We may pay this amortization payment in cash or in stock at the lower of \$0.75 per share or 80% of the volume weighted average price of our stock for the five trading days prior to the repayment date. In the event that we make the payment in cash, we shall pay 110% of the monthly redemption amount.

Except as provided in the succeeding paragraph and to the extent any debentures remain outstanding, at any time, the debentures are convertible into shares of our common stock at \$0.75 per share.

At any time after 90 days from the date that a registration statement registering the shares of common stock underlying the debentures and warrants is declared effective, and if certain conditions are met, we have the right to redeem some or all of the debentures in a cash amount equal to 110% of the face amount of the debentures being redeemed.

After the registration statement registering the shares of common stock underlying the debentures and warrants is declared effective, if the closing price for our common stock exceeds \$1.875 for 20 consecutive trading days, we can require the holders to convert some or all of the debentures at \$0.75.

In the event of default, the investors may require payment, which shall be the greater of: (A) 130% of the principal amount of the face amount of the debenture to be prepaid, or (B) the principal amount of the debenture to be prepaid, divided by the conversion price on (x) the date the default amount is demanded or otherwise due or (y) the date the default amount is paid in full, whichever is less, multiplied by the closing price on (x) the date the default amount is demanded or otherwise due or (y) the date the default amount is paid in full, whichever is greater.

We issued warrants to the investors, expiring September 21, 2008, to purchase 2,072,000 shares of restricted common stock, exercisable at a per share of \$0.80. In addition, the exercise price of the warrants will be adjusted in the event we issue common stock at a price below the exercise price, with the exception of any securities issued pursuant to a stock or option plan adopted by our board of directors, issued in connection with the debentures issued pursuant to the securities purchase agreement, or securities issued in connection with acquisitions or strategic transactions. Upon an issuance of shares of common stock below the exercise price, the exercise price of the warrants will be reduced to equal the share price at which the additional securities were issued and the number of warrant shares issuable will be

increased such that the aggregate exercise price payable for the warrants, after taking into account the decrease in the exercise price, shall be equal to the aggregate exercise price prior to such adjustment.

Warrants to purchase 100,000 shares, at the same price and for the same term as the warrants issued to the investors, have been issued to HPC Capital Management as additional compensation for its services in connection with the transaction with the investors.

After the effective date of this registration statement, if in any period of 20 consecutive trading days our stock price exceeds 250% of the warrants' exercise price, all of the warrants shall expire on the 30th trading day after we send a call notice to the warrant holders. If at any time after one year from the date of issuance of the warrants there is not an effective registration statement registering, or no current prospectus available for, the resale of the shares underlying the warrants, then the holder may exercise the warrant at such time by means of a cashless exercise. In the event the investors exercise the warrants on a cashless basis, then we will not receive any proceeds.

The conversion price of the debentures and the exercise price of the warrants may be adjusted in certain circumstances such as if we pay a stock dividend, subdivide or combine outstanding shares of common stock into a greater or lesser number of shares, or take such other actions as would otherwise result in dilution of the investors' position.

The investors have agreed to restrict their ability to convert their debentures or exercise their warrants and receive shares of our common stock such that the number of shares of common stock held by them in the aggregate and their affiliates after such conversion or exercise does not exceed 4.99% of the then issued and outstanding shares of common stock.

We agreed to file a registration statement with the Securities and Exchange Commission within 30 days of the effectiveness of the registration statement filed on August 10, 2005 (file no. 333-127413), which was declared effective on October 17, 2005, to cover the future sale by the investors of the shares issuable in payment and/or conversion of the debentures, and the shares issuable on exercise of the warrants. If the registration statement is not filed within such 30 day period or if the registration statement is not declared effective within 120 days from the date of filing, we are required to pay liquidated damages to the investors. The registration statement also will cover the future sale by HPC Capital Management of the shares issuable on exercise of the warrants issued to HPC in connection with the transaction.

### Sample Conversion Calculation

The number of shares of common stock issuable upon conversion of the convertible debentures is determined by dividing that portion of the principal of the convertible debentures to be converted by the conversion price. For example, assuming conversion of the \$3,108,000 of convertible debentures issued and outstanding on November 7, 2005, at a conversion price of \$0.4368, the number of shares issuable upon conversion would be:

$$\$3,108,000 / \$0.4368 = 7,115,385 \text{ shares}$$

The following is an example of the amount of shares of our common stock that are issuable, upon conversion of the principal amount of our convertible debentures, based on market prices 25%, 50% and 75% below the market price as of November 7, 2005 of \$0.54.

| <u>% Below Market</u> | <u>Price Per Share</u> | <u>With Discount at 20%</u> | <u>Number of Shares Issuable</u> | <u>% of Outstanding Stock</u> |
|-----------------------|------------------------|-----------------------------|----------------------------------|-------------------------------|
| 25%                   | \$ .405                | \$ .324                     | 9,592,593                        | 16.69%                        |
| 50%                   | \$ .27                 | \$ .216                     | 14,388,889                       | 23.11%                        |
| 75%                   | \$ .135                | \$ .108                     |                                  | 37.54%                        |

28,777,778

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**MARKET FOR COMMON EQUITY AND RELATED STOCKHOLDER MATTERS**

Our common stock is quoted on the OTC Bulletin Board under the symbol "FLWE". For the periods indicated, the following table sets forth the high and low bid prices per share of common stock. These prices represent inter-dealer quotations without retail markup, markdown, or commission and may not necessarily represent actual transactions.

|                         | High (\$) | Low (\$) |
|-------------------------|-----------|----------|
| <b>Fiscal Year 2003</b> |           |          |
| First Quarter           | \$0.15    | 0.15     |
| Second Quarter          | 0.15      | 0.15     |
| Third Quarter           | 0.15      | 0.05     |
| Fourth Quarter          | 1.90      | 0.04     |
| <b>Fiscal Year 2004</b> |           |          |
| First Quarter           | 2.23      | 1.10     |
| Second Quarter          | 1.63      | 0.81     |
| Third Quarter           | 1.12      | 0.69     |
| Fourth Quarter          | 1.02      | 0.71     |
| <b>Fiscal Year 2005</b> |           |          |
| First Quarter           | 1.25      | 0.71     |
| Second Quarter          | 1.00      | 0.42     |
| Third Quarter           | 1.40      | 0.48     |
| Fourth Quarter (1)      | 0.82      | 0.50     |

(1) As of November 9, 2005

**HOLDERS**

As of October 21, 2005, we had approximately 101 holders of our common stock. The number of record holders was determined from the records of our transfer agent and does not include beneficial owners of common stock whose shares are held in the names of various security brokers, dealers, and registered clearing agencies. The transfer agent of our common stock is Pacific Stock Transfer Company, 500 E. Warm Springs Road, Suite 240, Las Vegas, Nevada 89119.

We have never declared or paid any cash dividends on our common stock. We do not anticipate paying any cash dividends to stockholders in the foreseeable future. In addition, any future determination to pay cash dividends will be at the discretion of the Board of Directors and will be dependent upon our financial condition, results of operations, capital requirements, and such other factors as the Board of Directors deem relevant.

## **MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

Some of the information in this prospectus contains forward-looking statements that involve substantial risks and uncertainties. You can identify these statements by forward-looking words such as "may," "will," "expect," "anticipate," "believe," "estimate" and "continue," or similar words. You should read statements that contain these words carefully because they:

- discuss our future expectations;
- contain projections of our future results of operations or of our financial condition;
- and
- state other "forward-looking" information.

We believe it is important to communicate our expectations. However, there may be events in the future that we are not able to accurately predict or over which we have no control. Our actual results and the timing of certain events could differ materially from those anticipated in these forward-looking statements as a result of certain factors, including those set forth under "Risk Factors," "Business" and elsewhere in this prospectus. See "Risk Factors."

### **Overview**

On January 5, 2004, we began operations as an oil and gas exploration company. We acquired interests in certain assets owned by Diamond Oil & Gas Corporation, in exchange for 3,500,000 shares of common stock. The assets included certain oil and gas projects, as well as the right to enter into the Exploration Services Funding Agreement with Thomasson Partner Associates, Inc. of Denver, Colorado. Diamond is controlled by our CEO, George S. Young. The operations we plan for 2005 include exploring leases we have acquired as well as seeking to acquire and explore additional property. Our goal is to discover substantial commercial quantities of oil and gas, including coalbed methane, on the properties.

In February 2005 we amended our Exploration Services Agreement with Thomasson Partner Associates. Thomasson Partner Associates provides large-scale exploration opportunities to the oil and gas industry. By this agreement Thomasson Partner Associates provides to us the first right to review and purchase up to a 50% interest (as amended, a 100% interest beginning in February 2005) in oil and natural gas exploration projects developed by Thomasson Partner Associates. Under the agreement, in 2005, Thomasson Partner Associates will present to us a minimum of eight project opportunities with the reasonable potential of at least 200 Bcf of natural gas reserves or 20 million barrels of oil reserves. We have the first right to review exploration projects developed by Thomasson Partner Associates and, after viewing a formal presentation regarding a project, we have a period of thirty days in which to acquire up to 100% of the project. We are not obligated to acquire any project. In consideration, in 2004 we paid to Thomasson Partner Associates a \$400,000 overhead fee, and will pay an \$800,000 fee in 2005. We also pay a fee for each project we acquire from Thomasson Partner Associates. The agreement continues year to year until either party gives 90 days written notice of termination. Projects acquired from Thomasson Partner Associates include the Weston County project in Wyoming, the Gordon Creek project in Utah, the Carter Creek project in Wyoming, the Circus project in Montana and the Bacaroo project in Colorado. In 2004 we incurred charges from Thomasson Partner Associates totaling \$1,255,000, including the \$400,000 overhead fee.

### **Operations Plans**

During the next twelve months, we expect to pursue oil and gas operations on some or all of our property, including the acquisition of additional acreage through leasing, farmout or option and participation in the drilling of oil and gas wells. We intend to continue to evaluate additional opportunities in areas where we feel there is potential for oil and gas reserves and production and may participate in areas other than those already identified, although we cannot

assure that additional opportunities will be available, or if we participate in additional opportunities, that those opportunities will be successful.

Our current cash position is not sufficient to fund our cash requirements during the next twelve months, including operations and capital expenditures. We intend to continue equity and/or debt financing efforts to support our current and proposed oil and gas operations and capital expenditures. We may sell interests in our properties. We cannot assure that continued funding will be available.



We have not entered into commodity swap arrangements or hedging transactions. Although we have no current plans to do so, we may enter into commodity swap and/or hedging transactions in the future in conjunction with oil and gas production. We have no off-balance sheet arrangements.

Our future financial results continue to depend primarily on (1) our ability to discover or purchase commercial quantities of oil and gas; (2) the market price for oil and gas; (3) our ability to continue to source and screen potential projects; and (4) our ability to fully implement our exploration and development program with respect to these and other matters. We cannot assure that we will be successful in any of these activities or that the prices of oil and gas prevailing at the time of production will be at a level allowing for profitable production.

### **Recent Activity**

In February 2005 we agreed to sell the Circus project for \$1.98 million to an unrelated third party. We completed the sale in June 2005. We acquired the leases in October 2004, with a total cost through the sale of \$487,000. Additionally, we incurred \$53,000 of closing cost on the sale.

In February 2005 we extended our agreement with a financial consultant and are obligated to issue an additional 50,000 shares to the consultant for compensation for his services, as well as a monthly fee of \$7,500 for three months through April 2005. In April 2005, we further extended our agreement with the financial consultant through October 2005 on the same terms as the prior extension.

In March 2005 we agreed, subject to customary closing conditions, with Quaneco L.L.C. to acquire a 12.5% working interest in the Kirby and Castle Rock Coal Bed Natural Gas projects for \$3,850,000 in cash and one million dollars worth of shares of restricted common stock. Under the terms of the agreement, we will participate in a 48-well drilling program during 2005 on the Kirby project that will extend out from an existing 16-well pilot program of previously drilled wells. We will have ownership in the previously drilled wells, which are currently being dewatered and are expected to commence production in the near future. The other working interest owners in the Kirby project include Quaneco (25.0%), Pinnacle Gas Resources (50%) and Galaxy Energy Corporation (12.5%). We are currently seeking financing to fund our participation in this project.

On May 2, 2005, we entered into two option agreements with Thomasson Partner Associates to participate in the Platte and Badger projects located in Garden and Keith Counties, Nebraska, and Stanley and Hughes Counties, South Dakota, respectively. Under the agreements, the initial project fee is \$100,000 for the Platte project and \$150,000 for the Badger project. Upon execution of definitive agreements we will pay Thomasson Partner Associates \$80,000 for Platte, and \$105,000 for Badger. This amount represents approximately of the initial project fees plus reimbursement of Land Sat cost of \$30,000 each. In addition, there will be additional costs for a GeoChem survey on Platte and an air photo study on Badger for the amounts of \$13,000 and \$12,000, respectively. The total cost of these projects will be \$143,000 and \$217,000, respectively, by September 15, 2005.

On May 18, 2005, we closed on \$1,063,650 in equity financing and issued approximately 545,461 units, at a price of \$1.95 per unit, each unit consisting of 3.55 shares of our common stock, and one and one-half Series A warrants to purchase our common stock. The units were sold to a limited number of accredited investors through a private placement memorandum and were exempt from registration under the Securities Act, pursuant to Section 4(2) of the Securities Act. We also agreed to pay the following to a placement agent: (1) a placement fee equal to 10% of the gross proceeds received from sales to certain investors identified by the placement agent; (2) an option to purchase an amount of units equal to 15% of the units sold in the offering at a purchase price of \$1.95 per unit; (3) a warrant or warrants, identical to the warrants contained in the units, equal to 15% of the number of units issued to certain investors identified by the placement agent, and (4) a non-accountable expense allowance of 3% of the aggregate gross proceeds of the private placement.

Each whole warrant entitles the holder to purchase one share of our common stock for a price of \$1.00 per share for three years from the date of purchase of the unit. The warrants also contain limited anti-dilution rights. The warrants are subject to adjustment in the event of (1) any subdivision or combination of our outstanding common stock or (2) any distribution by us to holders of common stock of (x) a stock dividend, or (y) assets (other than cash dividends payable out of retained earnings) to holders of common stock. In addition, until two years from the date the registration statement filed pursuant to the Registration Rights Agreement is declared effective, and except for certain issuances of our common stock including (A) pursuant to rights, warrants, convertible securities or options outstanding on the date of issuance of the warrants, (B) pursuant to the private placement, or (C) in other limited circumstances, if and when we issue or sell any common stock (including rights, warrants, convertible securities or options for its capital stock) for a consideration per share less than the per share purchase price of such common stock in the private placement, then we shall issue additional common stock to the investors so that the average per share purchase price of the shares of common stock issued to the investors (of only the common stock still owned by such investors) is equal to such other lower price per share.

Pursuant to a Registration Rights Agreement that we entered into with the purchasers of the units, we granted registration rights for the purchased shares of common stock and the common stock issuable upon exercise of the warrants. We will pay certain expense incurred by the holders of the securities in exercising their registration rights. Additionally, we are obligated to prepare and file with the Commission a registration statement (on Form S-1 or SB-2, or other appropriate registration statement form) under the Securities Act, at our sole expense, so as to permit a resale of the shares purchased in the private placement, including those underlying the warrants, under the Securities Act by the investors as selling security holders (and not as underwriters).

The Registration Rights Agreement requires that we cause the registration statement to be filed within 30 calendar days from the first closing date with penalties of 2% per 30 day period for non-performance. In the event that (1) the registration statement is not declared effective within 90 calendar days from the first closing date, or (2) 120 days in the case of a review of the registration statement by the Commission, or (3) we do not maintain such registration statement as effective for the required period, then we will pay liquidated damages in common stock. Such payment of the liquidated damages shall not relieve us from our obligations to register the securities and the additional shares payable as liquidated damages.

The Registration Rights Agreement also requires that we will maintain the registration statement effective under the Securities Act until the earlier of (1) the date that none of the securities covered by such registration statement may be issued pursuant to the terms of such security, (2) the date that all of the securities have been sold pursuant to such registration statement, (3) the date the investors receive an opinion of our counsel, which counsel shall be reasonably acceptable to the investors, that the securities may be sold under the provisions of Rule 144 without limitation as to volume, (4) all securities have been otherwise transferred to persons who may trade such shares without restriction under the Securities Act, and we have delivered a new certificate or other evidence of ownership for such securities not bearing a restrictive legend, or (5) three years from the effective date of the registration statement. Piggyback registration rights apply if the registration statement is not effective during this period.

In June 2005, we paid off the balance on our \$1,500,000 loan to JMG Exploration, Inc., an affiliate of JED Oil, Inc., through the assignment of the our 50% interest in the Weston County and Gordon Creek projects.

## **Oil & Gas Projects**

### ***Weston County, Wyoming***

In November 2004 we executed a joint venture agreement with JMG Exploration, to drill our Weston County and Gordon Creek projects. Under the agreement, JMG Exploration will receive a 50% interest in exchange for spending \$2,000,000 in exploration and drilling activity on the two projects by November 7, 2005. In addition, JMG Exploration loaned \$1,500,000 to us with a short-term note. In connection with repayment of the JMG Exploration loan, we have assigned the remaining 50% interest in the Weston County project to JMG Exploration, subject to our right to reacquire those interests for approximately \$391,000 by June 30, 2005, which right has been exercised. As part of the full settlement of the \$1,500,000 note, JMG Exploration's commitment to spend \$2,000,000 in exploration and drilling activity by November 7, 2005 has been terminated. In connection with this transaction, we recorded a gain from extinguishment of debt of \$383,531.

The Weston County project is a 19,290-acre project on the east flank of the Powder River Basin. We anticipate that JMG Exploration will commence exploration, permitting and other pre-drilling activities in the second 2005 quarter. The prospect is a potential extension of an existing producing field. In addition, the parties will target the nearby locations with potential in the Minnelusa sandstone and Dakota channel sandstone formations.

### ***Gordon Creek, Utah***

JMG Exploration will also drill on the 5,242-acre Gordon Creek project, which we acquired from The Houston Exploration Company for \$288,000. The Gordon Creek project is in an area of known coal resources in Carbon County in eastern Utah near other operating coal bed methane projects, such as the Drunkard's Wash Project, which Our project personnel successfully drilled previously for River Gas Corporation.

Based on exploration results, JMG Exploration has indicated its intent to sell a portion of its working interest to Enterra Energy Trust in an arrangement under which JED Oil, Inc. under a development agreement with Enterra, will complete any development programs on the projects. In connection with repayment of the JMG Exploration loan, we have assigned the remaining 50% interest in the Gordon Creek project to JMG Exploration, subject to our right to reacquire those interests for approximately \$390,000 by June 30, 2005, which right has been exercised.

***Carter Creek, Wyoming***

In 2004 we purchased the 10,678-acre Carter Creek Project in the southern Powder River Basin. We plan to commence drilling in the near future at the project, in which we have a 100% working interest. Based on our analysis of the geologic structure of this region, we anticipate productive sections in the Cretaceous, Niobrara, Turner (Frontier) and Mowry layers, in that several existing wells in the Carter Creek area currently produce oil.

***Overthrust, Utah and Wyoming***

In 2004 we optioned the Overthrust project for a 65% working interest in 183,000 acres of oil, gas and coal bed methane leases in northeastern Utah and southwestern Wyoming from Quaneco, an Oklahoma company. We plan to test the three identified coal seams that run through much of the area. Previous drilling has included seven exploratory wells that identified multiple coal seams of Tertiary and Cretaceous age that appear to be prospective for coal bed methane. Some of the coal is of similar age and depositional condition to other productive coal bed methane fields.

We drilled our first well in the project in 2004, the Crane 6-7, in Rich County, Utah. The well reached a total depth of 4280 feet. We cored coal and carbonaceous shale over a combined interval of 556 feet. In September 2004 we received the results from the gas desorption tests from the Spring Valley coal of the Frontier formation and the coal in the Bear River formation in the well. Results showed 253 cubic feet of gas per ton on an ash-free basis in the coal in the well. Lesser amounts of gas were present in the carbonaceous shale in the well. These tests corroborate earlier data that was generated by Quaneco, our partner on the project, suggesting that coal in an area of the project that lies a considerable distance north of the Crane 6-7 may contain between 200 and 400 cubic feet of gas per ton. We have expensed the cost of this well as exploration expense, although we may choose to re-enter the well at a later date. The overall results indicate the potential for coal in a much wider area to contain economic levels of coal bed methane, and will help to further guide our ongoing logging, geologic and drilling operations. We believe the Overthrust project has attractive coal bed methane potential, although additional exploration activity will be necessary to prove up gas reserves.

***Bacaroo, Colorado***

In 2004 we optioned the Bacaroo project in Colorado through our affiliation with Thomasson Partner Associates. We believe the project is an opportunity to establish conventional oil and gas production with comparatively inexpensive drilling in areas of established production, while other projects being reviewed offer longer term, larger potential exploration opportunities. We are acquiring acreage in the prospect.

***Kirby and Castle Rock Projects, Powder River Basin, Montana***

In March 2005 we agreed, subject to customary closing conditions, with Quaneco to acquire a 12.5% working interest in the Kirby and Castle Rock Coal Bed Methane projects for \$3,850,000 in cash and one million dollars worth of shares of restricted common stock. We have paid \$500,000 toward the purchase, which vests in us a pro rata portion of the 12.5% interest, and we have until September 1, 2005 to pay additional amounts of the purchase price and vest in additional amounts. Under the terms of the agreement, we will participate in a 48 well drilling program during 2005 on the Kirby project that will extend out from an existing 16 well pilot program of previously drilled wells. We will have ownership in the previously drilled wells, which are currently being dewatered and are expected to commence production later in the near future. The other working interest owners in the Kirby project include Quaneco (25.0%),

Pinnacle Gas Resources (50%) and Galaxy Energy Corporation (12.5%).

We plan to participate in a 48 well drilling program during 2005 on the Castle Rock project that will extend out from four previously drilled core holes. The other working interest owners in the Castle Rock Project include Quaneco (25.0%), Enterra Energy Trust (43.75%), Carrizo (6.25%) and Galaxy Energy Corporation (12.5%).

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The Powder River Basin coalfield of northeastern Wyoming and southeastern Montana is an unconventional gas play that offers an unusual combination of comparatively moderate risk and large economic potential. The large coal deposits of the Powder River Basin are one of the greatest accumulations of coal in the world. These coal deposits contain a large resource of biogenic coal bed methane associated with numerous thick, laterally continuous, relatively shallow (less than 3,000 feet deep) Tertiary coal beds.

The Kirby project is an extension of the Powder River Basin coal bed methane play, which produces from the Tongue River Member of the Tertiary Fort Union Formation, on the western margin of the Basin north of Sheridan, Wyoming. This portion of the Basin has already seen considerable production from property owned and managed by Huber Oil & Gas at Prairie Dog Field which is on the Wyoming side, and Fidelity Oil & Gas at CX Field which straddles the Montana/Wyoming border. The Kirby project has 95,000 acres of fee, state and federal leasehold about 10 miles north of Decker, Montana. Fidelity's CX Field is about 6 miles south of the southern boundary of the prospect.

A 16-well pilot well program has been drilled on the Kirby acreage and is scheduled to begin production in the second 2005 quarter. This pilot program will test the productivity of the Wall and Flowers-Goodale coal formations. Gas content data from mud logs and cores taken over these zones indicates that the prospective coal is fully saturated with gas, which we believe will lead to a short period of dewatering before commercial gas production volume is achieved. The engineering firm Sproule Associates, Inc. has been retained to perform a resource evaluation of the Kirby project. We believe hundreds of wells could potentially be drilled on the 95,000-acre Kirby project.

The Castle Rock project is an extension of the Powder River Basin play on the eastern margin of the Basin north of Gillette, Wyoming. This portion of the Basin is where most of the Basin's production has occurred. The Castle Rock project has 140,000 acres of fee, state and federal leasehold along the Pumpkin Creek drainage about 20 miles west of Broadus, Montana. The eastern and northern boundaries of the prospect are the outcrops of the Sawyer and Flowers Goodale Coals. Sproule also conducted a resources evaluation of the Castle Rock project with favorable results.

#### ***Circus Project, Montana***

In May 2004, we optioned the Circus project through our affiliation with Thomasson Partner Associates. In February 2005 we agreed to sell the Circus project for \$1.98 million to an unrelated third party. We completed the sale in June 2005. We acquired the leases in October, 2004, with a total cost through the sale of \$487,000. Additionally, we incurred \$53,000 of closing cost on the sale.

#### ***Johns Valley Project, Utah***

In early 2004 we acquired an agreement with Johns Valley Limited Partnership whereby we have the option to earn 70% working interest in 25,201 acres of oil and gas leases from the Utah School and Institutional Trust Lands Administration. The option, which expired in October 2004, was for fifteen oil and gas leases that were for terms of ten years. Due to permitting delays and other operating parameters in the field, we are negotiating to restructure the potential option and the timing and amounts of our work commitments as provided under the option assignment agreement.

In mid-2004 we drilled the 10-33C2 well in this project to its planned depth of 1,365 feet. We drilled through a potentially productive coal seam. We cored the well and have sent the core to a lab for evaluation. We have expensed the cost of this well as exploration expense.

On April 14, 2005, we entered into a letter of intent to purchase the project, and we are under continuing negotiations to purchase the project or an interest in the project through an earn-in arrangement.

#### **Drilling Activity**

In 2004 we drilled an exploratory well on the Overthrust project, Utah and Wyoming, above, and an exploratory well on the Johns Valley Project, Utah, above. We drilled no development wells. We had no drilling activity prior to 2004.



## **Present Activity**

We described our present activity in detail by project in Oil and Gas Projects, above. We have interests in wells currently drilling in the Kirby and Castle Rock projects. Currently, we have interests in 16 wells that are commencing the production phase and in drilling programs with 96 wells during 2005. We also have plans to finance and drill on the Overthrust project, the Carter Creek project, the Bacaroo project and the Johns Valley project during 2005. We expect our partner, JMG Exploration, will also be drilling on the Weston County and Gordon Creek projects in 2005. We are seeking capital which we need in order to finance these projects.

## **Liquidity & Capital Resources**

In 2004 we incurred a loss of \$3,760,000. In the quarter ended June 30, 2005, we incurred a net loss of \$241,000. At June 30, 2005, we had \$2,503,000 of cash, total current assets of \$2,575,000 and current liabilities of \$332,000. In February 2005 we sold the Circus project for \$1.98 million to an unrelated third party. We acquired the leases in October, 2004, with a total cost through the sale of \$487,000. Additionally, we incurred \$53,000 of closing cost on the sale.

At March 31, 2005 we owed \$35,000 on an unsecured, 8% demand note payable to an entity controlled by our CEO. During the quarter ending June 30, 2005, we borrowed \$379,000 and paid down principal of \$414,000 on the note, resulting in the paying off of the remaining balance owed plus interest of \$500.

Based upon our significant operating losses from inception, there is substantial doubt as to our ability to continue as a going concern. Our audited and unaudited financial statements have been prepared on a basis that contemplates our continuation as a going concern and the realization of assets and liquidation of liabilities in the ordinary course of business. Our audited and unaudited consolidated financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts or the amounts and classification of liabilities that might be necessary should we be unable to continue as a going concern.

In the six months ended June 2005, we had net income attributable to the sale of an oil and gas property. From the inception of our oil and gas exploration business, we have not produced or sold any hydrocarbons. Although we have acquired an option of interest in the Kirby and Castle Rock projects which are now going into production, we have no assets at present which are able to generate oil and gas sales without further expenditures for the development of the reserves. Our ability to maintain profitability and positive cash flow is dependent upon our ability to exploit our mineral holdings, generate revenue from our planned business operations and control our exploration cost. To fully carry out our business plans we need to raise a substantial amount of additional capital, which we are currently seeking. We can give no assurance that we will be able to raise such capital. We have limited financial resources until such time that we are able to generate positive cash flow from operations. Our ability to maintain profitability and positive cash flow is dependent upon our ability to locate profitable natural gas or oil properties, generate revenue from our planned business operations, and control exploration cost. Should we be unable to raise adequate capital or to meet the other above objectives, it is likely that we would have to substantially curtail our business activity, and that our investors would incur substantial losses of their investment.

On May 18, 2005, we closed on the private placement of \$1,064,000 of securities. We incurred an estimated \$142,000 of fees and cost, netting approximately \$922,000. We sold 1,936,391 shares of common stock and 818,192 warrants. Each warrant entitles the holder to purchase one share of common stock for \$1.00 until May 18, 2008. We also issued 81,820 warrants to the placement agent as additional compensation to acquire the same units offered in the private placement

### *June 2005 Private Placement*

On June 17, 2005, we closed a financing pursuant to a securities purchase agreement with three accredited investors for the issuance of \$5,501,199.95 in face amount of debentures maturing September 16, 2008, and three year warrants to purchase our common stock. The debentures do not accrue interest and the investors paid \$3,849,685 for the debentures. A commission of 9% on the \$3,849,685 was paid by us to HPC Capital Management, a registered broker-dealer, in connection with the transaction, and we paid \$100,000 in expenses and fees including \$30,000 of the investors' counsel's legal fees, resulting in net proceeds to us of \$3,403,267.35. Net proceeds will be used by us for general working capital

The debentures are unsecured and we are obligated to pay 1/24th of the face amount of the debenture on the first of every month, starting October 1, 2005, which payment can be made in cash or in shares of our common stock. We may pay this amortization payment in cash or in stock at the lower of \$0.60 per share or 80% of the volume weighted average price of our stock for the five trading days prior to the repayment date. In the event that we make the payment in cash, we shall pay 110% of the monthly redemption amount.

Except as provided in the succeeding paragraph and to the extent any debentures remain outstanding, at any time, the debentures are convertible into shares of our common stock at \$0.60 per share.

At any time after 90 days from the date that a registration statement registering the shares of common stock underlying the debentures and warrants is declared effective, and if certain conditions are met, we have the right to redeem some or all of the debentures in a cash amount equal to 110% of the face amount of the debentures being redeemed.

After the registration statement registering the shares of common stock underlying the debentures and warrants is declared effective, if the closing price for our common stock exceeds \$1.50 for 20 consecutive trading days, we can require the holders to convert some or all of the debentures at \$0.60.

We issued warrants to the investors, expiring June 17, 2008, to purchase 4,584,334 shares of restricted common stock, exercisable at a per share of \$0.649. In addition, the exercise price of the warrants will be adjusted in the event we issue common stock at a price below the exercise price, with the exception of any securities issued pursuant to a stock or option plan adopted by our board of directors, issued in connection with the debentures issued pursuant to the securities purchase agreement, or securities issued in connection with acquisitions or strategic transactions. Upon an issuance of shares of common stock below the exercise price, the exercise price of the warrants will be reduced to equal the share price at which the additional securities were issued and the number of warrant shares issuable will be increased such that the aggregate exercise price payable for the warrants, after taking into account the decrease in the exercise price, shall be equal to the aggregate exercise price prior to such adjustment.

Warrants to purchase 250,000 shares, at the same price and for the same term as the warrants issued to the investors, have been issued to HPC Capital Management as additional compensation for its services in connection with the transaction with the investors.

After the effective date of the registration statement registering the shares of common stock underlying the debentures and warrants, if in any period of 20 consecutive trading days our stock price exceeds 250% of the warrants' exercise price, all of the warrants shall expire on the 30th trading day after we send a call notice to the warrant holders. If at any time after one year from the date of issuance of the warrants there is not an effective registration statement registering, or no current prospectus available for, the resale of the shares underlying the warrants, then the holder may exercise the warrant at such time by means of a cashless exercise. In the event the investors exercise the warrants on a cashless basis, then we will not receive any proceeds.

The conversion price of the debentures and the exercise price of the warrants may be adjusted in certain circumstances such as if we pay a stock dividend, subdivide or combine outstanding shares of common stock into a greater or lesser number of shares, or take such other actions as would otherwise result in dilution of the investors' position.

The investors have agreed to restrict their ability to convert their debentures or exercise their warrants and receive shares of our common stock such that the number of shares of common stock held by them in the aggregate and their affiliates after such conversion or exercise does not exceed 4.99% of the then issued and outstanding shares of common stock.

#### *September 2005 Private Placement*

On September 21, 2005, we closed a financing pursuant to a securities purchase agreement with two accredited investors for the issuance of \$3,108,000 in face amount of debentures maturing December 20, 2008, and three year warrants to purchase our common stock. The debentures do not accrue interest and the investors paid \$2,174,947.52 for the debentures. A commission of 8% on \$2,000,000 raised was paid by us to HPC Capital Management, a registered broker-dealer, in connection with the transaction and we placed \$50,000 in escrow for the payment of future legal fees in connection with our registration statement, resulting in net proceeds to us of \$1,964,947.52, before our

legal fees. Net proceeds will be used by us for general working capital.

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The debentures are unsecured and we are obligated to pay 1/24th of the face amount of the debenture on the first of every month, starting January 1, 2006, which payment can be made in cash or in shares of our common stock. We may pay this amortization payment in cash or in stock at the lower of \$0.75 per share or 80% of the volume weighted average price of our stock for the five trading days prior to the repayment date. In the event that we make the payment in cash, we shall pay 110% of the monthly redemption amount.

Except as provided in the succeeding paragraph and to the extent any debentures remain outstanding, at any time, the debentures are convertible into shares of our common stock at \$0.75 per share.

At any time after 90 days from the date that a registration statement registering the shares of common stock underlying the debentures and warrants is declared effective, and if certain conditions are met, we have the right to redeem some or all of the debentures in a cash amount equal to 110% of the face amount of the debentures being redeemed.

After the registration statement registering the shares of common stock underlying the debentures and warrants is declared effective, if the closing price for our common stock exceeds \$1.875 for 20 consecutive trading days, we can require the holders to convert some or all of the debentures at \$0.75.

We issued warrants to the investors, expiring September 21, 2008, to purchase 2,172,000 shares of restricted common stock, exercisable at a per share of \$0.80. In addition, the exercise price of the warrants will be adjusted in the event we issue common stock at a price below the exercise price, with the exception of any securities issued pursuant to a stock or option plan adopted by our board of directors, issued in connection with the debentures issued pursuant to the securities purchase agreement, or securities issued in connection with acquisitions or strategic transactions. Upon an issuance of shares of common stock below the exercise price, the exercise price of the warrants will be reduced to equal the share price at which the additional securities were issued and the number of warrant shares issuable will be increased such that the aggregate exercise price payable for the warrants, after taking into account the decrease in the exercise price, shall be equal to the aggregate exercise price prior to such adjustment.

Warrants to purchase 100,000 shares, at the same price and for the same term as the warrants issued to the investors, have been issued to HPC Capital Management as additional compensation for its services in connection with the transaction with the investors.

After the effective date of this registration statement, if in any period of 20 consecutive trading days our stock price exceeds 250% of the warrants' exercise price, all of the warrants shall expire on the 30th trading day after we send a call notice to the warrant holders. If at any time after one year from the date of issuance of the warrants there is not an effective registration statement registering, or no current prospectus available for, the resale of the shares underlying the warrants, then the holder may exercise the warrant at such time by means of a cashless exercise. In the event the investors exercise the warrants on a cashless basis, then we will not receive any proceeds.

The conversion price of the debentures and the exercise price of the warrants may be adjusted in certain circumstances such as if we pay a stock dividend, subdivide or combine outstanding shares of common stock into a greater or lesser number of shares, or take such other actions as would otherwise result in dilution of the investors' position.

The investors have agreed to restrict their ability to convert their debentures or exercise their warrants and receive shares of our common stock such that the number of shares of common stock held by them in the aggregate and their affiliates after such conversion or exercise does not exceed 4.99% of the then issued and outstanding shares of common stock.

**Cash flow.** In the June 2005 quarter we obtained \$189,000 in our operating activity. We used \$2,063,000 in investing activity for property and option acquisitions, and obtained \$4,228,000 in financing activity from capital obtained

through financings. We increased our March 31, 2005 cash balance of \$20,000 to \$2,503,000 at June 30, 2005.

## Results of Operations

**Revenue.** Throughout 2004 and 2005 to date, we earned no revenue from our exploration activity on our oil and gas property or from other operations.

**Operating expense.** For the quarter ended June 2005, our operating expense was \$582,000, compared to \$105,000 in the June 2004 quarter. The expense for both quarters came from oil and gas exploration, salaries, business advisory services, legal and professional fees, travel, occupancy and investor relations expense. The expense increased because of costs of capital and other business advisory services.

**Gain on sale of property.** In the March 2005 quarter we earned a \$1,437,000 gain on the sale of the Circus project, which we sold for \$1,977,000. Our cost on the leases was \$487,000. Additionally, we incurred \$53,000 of closing cost.

**Interest expense.** We incurred interest expense of \$48,000 in the June 2005 quarter compared to \$15,000 in the June 2004 quarter. Interest increased because of an increase in our debt between the two quarters.

## Critical Accounting Policies and Estimates

Our Management's Discussion and Analysis of Financial Condition and Results of Operations section discusses our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expense during the reporting period. On an on-going basis, we evaluate our estimates and judgments, including those related to revenue recognition, accrued expense, financing operations, contingencies and litigation. We base our estimates and judgments on historical experience and on various other factors that we believe to be reasonable under the circumstances. Our estimates and judgments form the basis for determining the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. These carrying values are some of the most significant accounting estimates inherent in the preparation of our financial statements. These accounting policies are described in relevant sections in this discussion and in the notes to the financial statements included in our December 31, 2004 Form 10-KSB Annual Report.

## BUSINESS

### Company History

Fellows Energy Ltd. (f/k/a Fuel Centers, Inc.) was incorporated in Nevada on April 9, 2001. In November 2001, the Commission declared effective our registration statement to register 31,185,150, as adjusted, shares of common stock held by our stockholders. We were originally formed to offer business consulting services in the retail automobile fueling industry. During the fourth quarter of 2003, we decided to change management, enter the oil and gas business and cease all activity in the automobile refueling industry. On November 12, 2003, we changed our name to Fellows Energy Ltd. and shifted our focus to exploration for oil and gas in the Rocky Mountain Region. Our common stock is publicly traded over-the-counter and quoted on the OTC Bulletin Board under the symbol "FLWE.OB."

We are an early stage oil and gas company led by an experienced management team and focused on exploration and production of natural gas, especially from "unconventional plays" such as tight sands and coal beds, and oil in the Rocky Mountain Region. In many unconventional plays accumulations of hydrocarbons are found over a large areal expanse and/or a thick vertical section, which when compared to conventional plays, typically have a higher geological and/or commercial development risk and lower average decline rate. Whereas a "conventional play" is an accumulation of hydrocarbons in a structural or stratigraphic setting within high-quality reservoirs. Our strategy is to pursue selected opportunities that are characterized by reasonable entry costs, favorable economic terms, high reserve potential relative to capital expenditures and the availability of existing technical data that may be further developed using current technology.

On January 5, 2004, we acquired certain interests in certain oil and gas leases and other interests owned by Diamond Oil & Gas Corporation, a Nevada corporation. Diamond is wholly owned by George S. Young, our CEO, President and a Director.

In connection with the transaction with Diamond, we (1) issued 3,500,000 shares of our common stock to Diamond; (2) completed a private placement of \$2,750,000, pursuant to which we issued 2,750,000 shares of our common stock at \$1.00 per share; (3) appointed George S. Young as our President, Chief Executive Officer and a Director and Steven L. Prince as our Vice President and a Director; and (4) accepted the resignation of our then management and redeemed 52,610,000 shares of our common stock owned by the outgoing and former management in exchange for an aggregate sum of \$27,000.

### Business Strategy

We seek to: (1) achieve attractive returns on capital for the benefit of our stockholders through investment in exploration and development of unconventional plays; (2) maintain a strong balance sheet to preserve maximum financial and operational flexibility; and (3) create strong employee incentives through equity ownership.

#### *Focus on Unconventional Coal Bed Methane and Tight Gas Sand Plays*

We plan to continue our focus on coal bed methane and tight gas sand plays in the Rocky Mountain Region.

In our short operating history in the oil and gas industry, we have positioned Fellows to control and exploit potential reserves from a number of large oil and gas projects. These projects focus on coal bed methane, tight sands gas and oil from fractured shales and are characterized by their widespread occurrence, large reserve potential, low finding and development costs, high drilling success rates, and low geologic and operating risks. The current project portfolio highlights our ability to negotiate deals where it controls such opportunities with relatively small amounts of capital. If we can establish that a particular play has commercial oil and/or gas reserves, the associated land position takes on substantial value as the resource is translated into proven reserves through development drilling. If we can achieve large proven reserves that result from initial drilling success, then we could have the ability to raise debt financing for



development of the field.

We also plan to include conventional oil and gas projects in its mix to create cash flow and reserves in the short term to support our overhead and allow for orderly development of the larger, more capital and lead-time intensive unconventional projects.

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We believe the Powder River Basin (located in Wyoming and Montana), Overthrust Belt (located in Utah and Wyoming) and Uinta Basin (located in Utah) represent some of the most attractive regions for unconventional plays in North America due to a combination of available land, large unconventional play opportunities, low finding and development cost and production potential. Moreover, because of these regions' proximity to major pipeline networks serving important U.S. markets, price differentials for gas sales can be managed at acceptable levels.

### ***Disciplined Acquisition Strategy***

We intend to acquire producing oil and gas properties where we believe significant additional value can be created. Management is primarily interested in unconventional play properties with a combination of these factors: (1) opportunities for long life production with stable production levels; (2) geological formations with multiple producing horizons; (3) substantial exploitation potential; and (4) relatively low capital investment production costs.

### ***Exploitation of Properties***

We intend to maximize the value of our properties through a combination of successful exploration, drilling, increasing production, increasing recoverable reserves and reducing operating costs. Where we deem appropriate, we will employ technology to improve recoveries such as directional and horizontal drilling. Directional and horizontal drilling and completion methods have historically produced oil and gas at faster rates and with lower operating costs basis than traditional vertical drilling.

### ***Experienced and Incentivized Personnel***

We intend to maintain a highly competitive team of experienced and technically proficient employees and consultants and motivate them through a positive work environment and stock ownership. We believe that employee ownership, which is encouraged through our stock option plan, is essential for attracting, retaining and motivating qualified personnel.

### ***Stock Option Plan***

On October 9, 2003, we adopted an incentive stock option plan, pursuant to which shares of our common stock are reserved for issuance to satisfy the exercise of options. The purpose of the incentive stock option plan is to retain qualified and competent officers, employees and directors. The incentive stock option plan for our executive officers authorizes up to 2,000,000 shares of common stock, to be purchased pursuant to the exercise of options. The effective date of the stock option plan was October 9, 2003, and the stock option plan was approved by our shareholders on November 10, 2003. On September 15, 2004, we granted an option for 200,000 shares to our CEO, 150,000 shares to our Vice President and 125,000 shares to an employee. These options are exercisable at \$0.80 per share, the price of our common stock on the date of grant. The options vested 50% on the grant date and will vest 50% on September 15, 2005.

### **Company and Industry Highlights**

#### ***Solid Rocky Mountain Fundamentals***

According to the report *Balancing Natural Gas Policy - Fueling Demands of a Growing Economy* (September 25, 2003), released in the fall of 2003 by the National Petroleum Council:

current higher gas prices are the result of a fundamental shift in the supply and demand balance. North America is moving to a period in its history in which it will no longer be self-reliant in meeting its growing natural gas needs as production from traditional U.S. and Canadian basins has plateaued. Government policy encourages the use of natural

gas but does not address the corresponding need for additional natural gas supplies.

Furthermore, within the State of Wyoming, as indicated by data compiled by the Wyoming Oil & Gas Conservation Commission and available on its website at [www.wogcc.state.wy.us](http://www.wogcc.state.wy.us), gas production has increased 80% since the mid-1990s and is expected to surpass 6 Bcf per day this year, largely from coal bed methane production in the Powder River Basin and tight sands gas production from the Green River Basin. In the Powder River Basin, 16,000 wells have been drilled to date (mostly in the last five years) and approximately 50,000 additional drill locations have been identified. Although this area has been historically challenged by pipeline capacity restraints and tough environmental regulations, substantial progress has been made with the doubling of capacity of the Kern River Pipeline and the completion of the Grasslands and Cheyenne Plains Pipelines, which Management believes bodes well for future development, growth and economics in the Rocky Mountain Region.

### ***Focus on Unconventional Plays***

In building our inventory of oil and gas projects, we have concentrated primarily on unconventional plays.

Compared to conventional plays, unconventional plays present different advantages and risks. Typically, unconventional plays involve less geologic risk than conventional plays with respect to locating gas because hydrocarbons are known to exist and because unconventional plays are typically larger in size. Similarly, due to the greater size of typical unconventional plays, they inherently have greater reserve potential than conventional plays. In general, unconventional plays have not been developed to the extent of conventional plays and therefore greater opportunities exist for acquiring additional unconventional plays and increasing reserves.

However, development of typical unconventional plays may involve greater extraction and retrieval costs than are involved in development of typical conventional plays. In the typical unconventional play, the existence of gas is known but the quantity of such gas, and commercial viability, is unknown. The process of developing an unconventional play requires significant costs before the commercial viability can be ascertained. Therefore, there is a greater risk of cost overrun and the risk of inadequate gas recoveries is not avoided.

It is important to recognize that unconventional plays offer attractive potential for large reserve additions. This is because the large conventional traps have largely been found and developed, and because unconventional plays inherently have much greater size and therefore greater reserve potential. All of the top five onshore “gas giant” fields discovered and developed in the 1990s (including Powder River Basin coal bed methane, Jonah, Pinedale, Madden Deep and Ferron coal bed methane) were in the Rocky Mountain Region. Four out of the five with estimated reserves of over 30 TCF were unconventional tight sands or coal bed methane unconventional plays.

### ***Strong Acquisition Market***

The recent sales of major Rocky Mountain independent oil and gas companies such as Westport Resources Corporation, Tom Brown, Inc., Evergreen Resources, Inc., Patina Oil & Gas Corporation and Prima Energy Corporation for total consideration of over ten billion dollars, in the opinion of our management, bear testimony to the strength of the acquisition market for companies that have established proven reserve growth from unconventional plays. While only Evergreen was a pure unconventional-play oriented company, each of the others has had a major component of such plays as part of their portfolio which helped to increase their exit valuations due to the large amount of proven undeveloped category reserves associated with them. Although there are no assurances, we anticipate that the success of any of our major unconventional plays will quickly make it a favored acquisition target for large, public companies seeking to grow through strategic acquisitions, thus providing an attractive exit strategy for our stockholders.

### ***Large Strategic Land Position***

Through our direct ownership of mineral rights in the Powder River Basin, Overthrust Belt and Uinta Basin, we have a strategic land position in the oil and gas producing basins of the Rocky Mountains. Known hydrocarbon resources in reservoirs in unconventional plays such as coal seams, thick oil-bearing shales, and extensive bodies of tight gas-bearing sands throughout the properties create the potential for a large inventory of drilling locations should initial exploration efforts prove successful. Although there are no assurances, this inventory could support future net reserve additions and production growth over the next several years.

### ***Strong Underlying Industry Fundamentals***

According to the National Petroleum Council Gas Report, the domestic natural gas fundamentals will continue to be attractive, for the foreseeable future. The U.S. faces a significant natural gas supply problem due to the maturing of its traditional producing basins, the increase in exploration and development costs, and demand increases coupled with

production decline rates. The U.S. has several ways to combat this supply problem through measures including increased development and importation of Canadian and Alaskan gas and delivery of liquefied natural gas. However, the impact of these efforts is expected to only mitigate the supply decline or at best increase supply marginally.

### ***Proven Management Expertise***

Our CEO and President George S. Young and our Vice President Steve Prince have experience in operating and growing an oil and gas public company. Mr. Young brings strong leadership and business qualifications, an understanding from having been trained as both an attorney and engineer and 25 years of natural resource industry experience. Mr. Prince brings 13 years of oil and gas industry experience as a geologist and as a significant contributor to the development of major producing fields in areas of interest to us.

### **Financing Strategy**

We intend to access debt and equity markets for private and public financings from time to time based on our needs on terms in the market then available to us. Initially, we expect that the bulk of capital formation will be in the form of equity capital to support the initial phases of exploration and exploitation work required on our projects. To the extent the plays mature into “Proven” status as determined by independent third-party engineers, we plan to utilize debt sources for a large percentage of our capital requirements so as to maximize the return on equity that these projects generate. This debt may be in the form of senior bank debt, junior or subordinated bank debt, and/or mezzanine debt. We cannot provide any assurance that we will be able to raise additional debt or equity to fund future operational and exploration needs or terms acceptable to us.

Additionally, we may generate funds through (1) a joint venture, sale or farm out on an interest in one or more of its properties and/or (2) divesting one or more of our properties that are determined not to fit with its strategic core holdings. On November 8, 2004, we entered into a joint venture agreement with JMG Exploration and Enterra Energy Trust in which the parties will receive a 50% interest in certain of our properties in exchange for a \$2,000,000 commitment for exploration and drilling on such properties.

### **Property Summary**

In our short operating history in the oil and gas industry, we have positioned Fellows to control and exploit potential reserves from a number of large unconventional oil and gas resource type projects covering approximately 456,000 gross and 180,000 net acres. These projects focus on coal bed methane, tight sands gas and oil from fractured shales. Such projects are characterized by their widespread occurrence, large reserve potential, low finding and development costs, high drilling success rates, and low geologic and operating risks. Such projects are also subject to certain risks and development of such projects requires substantial capital.

### **Competition**

Oil and gas exploration and acquisition of undeveloped properties is a highly competitive and speculative business. We compete with a number of other companies, including major oil companies and other independent operators which are more experienced and which have greater financial resources. Such companies may be able to pay more for prospective oil and gas properties. Additionally, such companies may be able to evaluate, bid for and purchase a greater number of properties and prospects than our financial and human resources permit. We do not hold a significant competitive position in the oil and gas industry.

### **Regulation**

Our operations are or will be subject to various types of regulation at the federal, state and local levels. Such regulation includes requiring permits for the drilling of wells; maintaining bonding requirements in order to drill or operate wells; implementing spill prevention plans; submitting notification and receiving permits relating to the presence, use and release of certain materials incidental to oil and gas operations; and regulating the location of wells, the method of drilling and casing wells, the use, transportation, storage and disposal of fluids and materials used in connection with drilling and production activities, surface usage and the restoration of properties upon which wells

have been drilled, the plugging and abandoning of wells and the transporting of production. Our operations are or will be also subject to various conservation matters, including the regulation of the size of drilling and spacing units or proration units, the number of wells which may be drilled in a unit, and the unitization or pooling of oil and gas properties. In this regard, some states allow the forced pooling or integration of tracts to facilitate exploration while other states rely on voluntary pooling of lands and leases, which may make it more difficult to develop oil and gas properties. In addition, state conservation laws establish maximum rates of production from oil and gas wells, generally limit the venting or flaring of gas, and impose certain requirements regarding the ratable purchase of production. The effect of these regulations is to limit the amounts of oil and gas we may be able to produce from our wells and to limit the number of wells or the locations at which we may be able to drill.

Our business is affected by numerous laws and regulations, including energy, environmental, conservation, tax and other laws and regulations relating to the oil and gas industry. We plan to develop internal procedures and policies to ensure that our operations are conducted in full and substantial environmental regulatory compliance.

Failure to comply with any laws and regulations may result in the assessment of administrative, civil and criminal penalties, the imposition of injunctive relief or both. Moreover, changes in any of these laws and regulations could have a material adverse effect on business. In view of the many uncertainties with respect to current and future laws and regulations, including their applicability to us, we cannot predict the overall effect of such laws and regulations on our future operations.

We believe that our operations comply in all material respects with applicable laws and regulations and that the existence and enforcement of such laws and regulations have no more restrictive an effect on our operations than on other similar companies in the energy industry. We do not anticipate any material capital expenditures to comply with federal and state environmental requirements.

### **Environmental Matters**

Operations on properties in which we have an interest are subject to extensive federal, state and local environmental laws that regulate the discharge or disposal of materials or substances into the environment and otherwise are intended to protect the environment. Numerous governmental agencies issue rules and regulations to implement and enforce such laws, which are often difficult and costly to comply with and which carry substantial administrative, civil and criminal penalties and in some cases injunctive relief for failure to comply.

Some laws, rules and regulations relating to the protection of the environment may, in certain circumstances, impose “strict liability” for environmental contamination. These laws render a person or company liable for environmental and natural resource damages, cleanup costs and, in the case of oil spills in certain states, consequential damages without regard to negligence or fault. Other laws, rules and regulations may require the rate of oil and gas production to be below the economically optimal rate or may even prohibit exploration or production activities in environmentally sensitive areas. In addition, state laws often require some form of remedial action, such as closure of inactive pits and plugging of abandoned wells, to prevent pollution from former or suspended operations.

Legislation has been proposed in the past and continues to be evaluated in Congress from time to time that would reclassify certain oil and gas exploration and production wastes as “hazardous wastes.” This reclassification would make these wastes subject to much more stringent storage, treatment, disposal and clean-up requirements, which could have a significant adverse impact on operating costs. Initiatives to further regulate the disposal of oil and gas wastes are also proposed in certain states from time to time and may include initiatives at the county, municipal and local government levels. These various initiatives could have a similar adverse impact on operating costs.

The regulatory burden of environmental laws and regulations increases our cost and risk of doing business and consequently affects our profitability. The federal Comprehensive Environmental Response, Compensation and Liability Act, or CERCLA, also known as the “Superfund” law, imposes liability, without regard to fault, on certain classes of persons with respect to the release of a “hazardous substance” into the environment. These persons include the current or prior owner or operator of the disposal site or sites where the release occurred and companies that transported, disposed or arranged for the transport or disposal of the hazardous substances found at the site. Persons who are or were responsible for releases of hazardous substances under CERCLA may be subject to joint and several liability for the costs of cleaning up the hazardous substances that have been released into the environment and for damages to natural resources, and it is not uncommon for the federal or state government to pursue such claims.



It is also not uncommon for neighboring landowners and other third parties to file claims for personal injury or property or natural resource damages allegedly caused by the hazardous substances released into the environment. Under CERCLA, certain oil and gas materials and products are, by definition, excluded from the term “hazardous substances.” At least two federal courts have held that certain wastes associated with the production of crude oil may be classified as hazardous substances under CERCLA. Similarly, under the federal Resource, Conservation and Recovery Act, or RCRA, which governs the generation, treatment, storage and disposal of “solid wastes” and “hazardous wastes,” certain oil and gas materials and wastes are exempt from the definition of “hazardous wastes.” This exemption continues to be subject to judicial interpretation and increasingly stringent state interpretation. During the normal course of operations on properties in which we have an interest, exempt and non-exempt wastes, including hazardous wastes, that are subject to RCRA and comparable state statutes and implementing regulations are generated or have been generated in the past. The federal Environmental Protection Agency and various state agencies continue to promulgate regulations that limit the disposal and permitting options for certain hazardous and non-hazardous wastes.

We believe that the operator of the properties in which we have an interest is in substantial compliance with applicable laws, rules and regulations relating to the control of air emissions at all facilities on those properties. Although we maintain insurance against some, but not all, of the risks described above, including insuring the costs of clean-up operations, public liability and physical damage, there is no assurance that our insurance will be adequate to cover all such costs, that the insurance will continue to be available in the future or that the insurance will be available at premium levels that justify our purchase. The occurrence of a significant event not fully insured or indemnified against could have a material adverse effect on our financial condition and operations. Compliance with environmental requirements, including financial assurance requirements and the costs associated with the cleanup of any spill, could have a material adverse effect on our capital expenditures, earnings or competitive position. We do believe, however, that our operators are in substantial compliance with current applicable environmental laws and regulations. Nevertheless, changes in environmental laws have the potential to adversely affect operations. At this time, we have no plans to make any material capital expenditures for environmental control facilities.

## **EMPLOYEES**

As of the date of this prospectus, we have 4 full-time employees. The majority of development services have been provided to us by the officers and outside, third-party vendors. Currently, there exist no organized labor agreements or union agreements between us and our employees. We do not have employment agreements with any of our employees. We believe that our relations with our employees are good.

## **DESCRIPTION OF PROPERTIES**

Our principal executive offices are located at 370 Interlocken Boulevard, Suite 400, Broomfield, Colorado 80021, and our telephone number is (303) 327-1525. We occupy approximately 2,500 square feet of office space under a lease expiring in February 2006. The monthly rent is \$3,300. We believe that our current office space and facilities are sufficient to meet our present needs and do not anticipate any difficulty securing alternative or additional space, as needed, on terms acceptable to us. In addition, we have the following properties in connection with our business activities:

### **Overthrust Coal Bed Methane Project, Utah and Wyoming**

The Overthrust Coal Bed Methane Project is an unconventional play with 183,000 gross and 118,950 net acres targeting coal bed natural gas in southwestern Wyoming and northeastern Utah. This project also has the potential for conventional oil and gas.

In March 2004, Fellows entered into an option agreement with Quaneco, L.L.C., an Oklahoma limited liability company, to acquire a 65% working interest for \$250,000 in the Overthrust Coal Bed Methane Project. The

Overthrust Coal Bed Methane Project is located in Rich and Summit Counties of northeastern Utah, and Uinta County, Wyoming. Quaneco has approximately 183,000 acres under lease in the project area. Just east of the project area is over 6 TCF of gas production from the conventional "Overthrust" oil and gas play, so pipeline infrastructure and gas markets are well established in the area.

Under the terms of the option agreement with Quaneco, we have paid to Quaneco an option payment of \$100,000 and issued 200,000 shares of common stock in early 2005. We are presently renegotiating the balance of the terms of our earn-in agreement with Quaneco based on our work performed to date, as described.

Based upon regional geologic studies of historical oil and gas and coal mining activity, plus the results from seven exploratory wells previously drilled by Quaneco, the Overthrust coal bed methane play has multiple coal seams of Tertiary and Cretaceous age that may contain coal bed methane. Some of this coal is of similar age and depositional condition to other productive coal bed methane fields such as the Drunkard's Wash field in eastern Utah which has estimated reserves of 2 TCF.

In May 2004, we completed the first round of our exploratory activity with the drilling of the Crane #6-7 Well on the northern portion of the Overthrust Coal Bed Methane Project lease block in northern Utah. The well reached a depth of 4,280 feet. we cored coals and carbonaceous shales over a combined interval of 556 feet. The core tests confirm the presence of coals with potentially commercial gas contents in the Frontier and Bear River formations.

In the balance of 2005, we plan to conduct the second round of exploration activities on project, which will include well log analysis, seismic analysis and the purchase of additional seismic information, and the preparation of drill site locations and permitting for additional drilling to target not only the coal bed methane potential, but also the conventional gas sands that have been encountered in the previous exploration work. This activity may also include activity in the southern portion of the project, including detailed geologic studies of the Coalville and Henrys Fork areas, core drilling, and production testing. The Coalville and Henrys Fork area contains known thick coals in the Tertiary Adaville and Cretaceous Frontier formations. These coals crop out and are mined in and around the small town of Coalville, Utah. Wells in the Coalville area were reported to have penetrated net coal thickness of 100 feet from the Adaville Formation and 50 feet from the Frontier Formation. The State of Utah estimates the gas-in-place (coal bed methane gas resource) could range from 0.1 to 1.0 TCF from the Tertiary Adaville and Cretaceous Frontier formations.

#### **Kirby Coal Bed Methane Project, Big Horn & Custer Counties, Montana**

In March 2005, we entered into an option agreement with Quaneco to acquire a 12.5% working interest for \$2,225,000 in the Kirby Coal Bed Methane Project. This option agreement provides that \$458,763 of the purchase price will be in the form of our common stock valued at \$0.60 per share. The balance of the purchase price of \$1,766,237 is in cash due by September 1, 2005. We have paid an aggregate amount of \$500,000 toward the cash components of the purchase price of the Kirby and Castle Rock projects. In the event we do not complete the balance of the cash payments, we will nonetheless be vested in a pro rata portion of the 12.5% interest in each project in proportion to the amount actually paid. Pursuant to this agreement, we will participate in a 48 well drilling program during 2005 that will extend out from an existing 18 well pilot program of previously drilled wells. Our share of the 48 well drilling program is projected at \$562,500. We will have ownership in the previously drilled wells, which are currently being dewatered. The other working interest owners in the Kirby Coal Bed Methane Project include Quaneco (25%), Pinnacle Gas Resources (50%), and Galaxy Energy Corporation (OTCBB: GAXI) (12.5%).

The Powder River Basin coalfield of northeastern Wyoming and southeastern Montana is an unconventional gas play that offers an unusual combination of reasonable risk and large economic potential. The vast coal deposits of the Powder River Basin are one of the greatest accumulations of coal in the world. These coal deposits contain a large resource of biogenic coal bed natural gas associated with numerous thick, laterally continuous, relatively shallow (less than 3,000 feet deep) Tertiary coal beds.

The Kirby Coal Bed Methane Project is an extension of the Powder River Basin Coal Bed Methane play, which produces from the Tongue River Member of the Tertiary Fort Union Formation, on the western mar