

Citadel Exploration, Inc.
Form 8-K
May 13, 2011

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

Form 8-K

CURRENT REPORT

Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Date of Report (Date of earliest event reported) May 3, 2011

CITADEL EXPLORATION, INC.
(Exact name of registrant as specified in its charter)

Nevada (State or other jurisdiction of incorporation)	333-164850 (Commission File Number)	27-1550482 (IRS Employer Identification No.)
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420 Bryant Circle, Unit D, Ojai, California (Address of Principal Executive Offices)	93023 (Zip Code)
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Registrant's telephone number, including area code: (805) 218-9785

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Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions:

Written communications pursuant to Rule 425 under the Securities Act (17 CFR 230.425)

Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 CFR 240.14a-12)

Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b))

Pre-commencement communications pursuant to Rule 13e-4(c) under the Exchange Act (17 CFR 240.13e-4(c))

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Current Report on Form 8-K contains forward-looking statements. All statements other than statements of historical fact are “forward-looking statements” for purposes of federal and state securities laws, including, but not limited to, any perceived benefits as the result of the Membership Purchase Agreement and Plan of Reorganization referenced herein, any projections of earnings, revenue or other financial items; any statements of the plans, strategies and objections of management for future operations; any statements concerning proposed new services or developments; any statements regarding future economic conditions or performance; any statements or belief; and any statements of assumptions underlying any of the foregoing.

This Current Report includes statements regarding our plans, goals, strategies, intent, beliefs or current expectations. These statements are expressed in good faith and based upon a reasonable basis when made, but there can be no assurance that these expectations will be achieved or accomplished. These forward-looking statements can be identified by the use of terms and phrases such as “believe,” “plan,” “intend,” “anticipate,” “target,” “estimate,” “expect,” “like, and/or future-tense or conditional constructions (“will,” “may,” “could,” “should,” etc.). Items contemplating or making assumptions about actual or potential future sales, subscriptions, market size, collaborations, and trends or operating results also constitute such forward-looking statements.

Although forward-looking statements in this report reflect the good faith judgment of management, forward-looking statements are inherently subject to known and unknown risks, business, economic and other risks and uncertainties that may cause actual results to be materially different from those discussed in these forward-looking statements. Readers are urged not to place undue reliance on these forward-looking statements, which speak only as of the date of this report. We assume no obligation to update any forward-looking statements in order to reflect any event or circumstance that may arise after the date of this report, other than as may be required by applicable law or regulation. Readers are urged to carefully review and consider the various disclosures made by us in our reports filed with the Securities and Exchange Commission (“SEC”) which attempt to advise interested parties of the risks and factors that may affect our business, financial condition, results of operation and cash flows. If one or more of these risks or uncertainties materialize, or if the underlying assumptions prove incorrect, our actual results may vary materially from those expected or projected.

EXPLANATORY NOTE

On March 2, 2011, the Registrant changed its name from Subprime Advantage, Inc. to Citadel Explorations, Inc. in anticipation of the completion of the acquisition of 100% of all of the outstanding membership interest of Citadel Exploration, LLC. The acquisition of 100% of the outstanding membership interest of the mentioned limited liability company was completed on May 3, 2011. As a result of the completion of the acquisition, the Registrant is now an oil and gas exploration and production company.

References throughout this Current Report on Form 8-K to “we,” “our,” “us,” “the Company,” “the Registrant,” “Citadel,” similar terms refer to Citadel Exploration, Inc., unless otherwise expressly stated or the context otherwise requires. This Current Report contains summaries of the material terms of the agreements executed in connection with the transactions described herein. The summaries of these agreements are subject to, and qualified in their entirety by, reference to those agreements, all of which are incorporated herein by reference.

Section 1 – Registrant’s Business and Operations

Item 1.01 Entry into a Material Definitive Agreement.

As previously reported by the Registrant in its Current Report on Form 8-K, filed on March 1, 2011, the Registrant entered into a Membership Purchase Agreement and Plan of Reorganization (the “Agreement”) with Citadel Exploration, LLC, a California Limited Liability Company (“CEL”) on February 28, 2011 to acquire one hundred percent (100%) of CEL’s outstanding membership interest in exchange for Fourteen Million (14,000,000) shares of the Registrant’s common stock. The acquisition was completed on May 3, 2011. See Item 2.01 below for a further description of the acquisition.

Section 2 – Financial Information

Item 2.01 Completion of Acquisition or Disposition of Assets.

On May 3, 2011, we completed the acquisition of 100% of the outstanding membership interest of CEL pursuant to the Membership Purchase Agreement and Plan of Reorganization described in Item 1.01 above and in this Item 2.01. The acquisition was accounted for as a recapitalization effected by an exchange of shares for the assets, wherein Citadel Exploration, LLC is considered the acquirer for accounting and financial reporting purposes.

Pursuant to the terms of the Agreement, the Registrant accepted the resignation of its prior officers and director and appointed Michael J. Finch as Chief Executive Officer, President, and a Director, Daniel L. Szymanski as Chairman of the Board, Christopher M. Whitcomb as Chief Financial Officer and a Director, James Borgna as a Director, and Jacob L. Barnhart as a Director of the Registrant.

Pursuant to the conditions to closing of the Membership Purchase Agreement and Plan of Reorganization, the Registrant issued 14,000,000 shares of common stock in exchange for 100% of the outstanding membership interest of CEL and obtained cancellation of 7,690,000 affiliate shares of common stock.

FORM 10 DISCLOSURE

We are providing below the information that would be included in a Form 10 if we were to file a Form 10. Please note that the information provided below relates to the current operations acquired through the closing of the Membership Purchase Agreement and Plan of Reorganization discussed above.

DESCRIPTION OF BUSINESS

As a result of the closing of the Membership Purchase Agreement and Plan of Reorganization discussed in Items 1.01 and 2.01 above, our main focus has been redirected to the oil and gas exploration and production business. The information set forth herein is only a summary of our business plans.

INDUSTRY AND MARKET DATA

The market data and certain other statistical information used throughout this report are based on independent industry publications, government publications, reports by market research firms or other published independent sources. In addition, some data are based on our good faith estimates.

Business Development

Citadel Exploration, Inc. ("Citadel") was formed as a Nevada corporation in December 2009. On March 2, 2011, Citadel changed its name from Subprime Advantage, Inc. to Citadel Exploration, Inc. Effective May 3, 2011, Citadel completed the acquisition of the Indian Shallow Oil Development Project, located in the Bitterwater sub-basin of the Salinas Basin in California, consisting of 688.71 acres of leased property from Vintage Petroleum, LLC, a division of Occidental Petroleum, through the acquisition of 100% of the outstanding membership interest of CEL (more fully described in Item 2.01 above).

As a result of the closing of the Membership Purchase Agreement and Plan of Reorganization, Citadel is an oil and gas exploration company with operations in the Salinas Basin of California. As a result of our recent acquisition of CEL, we will have a broad portfolio of capital investment opportunities that arise from CEL's extensive knowledge of the geology and the history of oil and gas exploration and development in California as well as long-term presence and familiarity and relationships with other companies engaged in oil and gas industry in California.

Recent Change in Management

As a result of the closing of the Membership Purchase Agreement, we accepted the resignation of our prior sole officer and director and appointed Michael J. Finch as Chief Executive Officer, President and a Director, Daniel L. Szymanski as Chairman of the Board, Christopher M. Whitcomb as Chief Financial Officer and a Director, James Borgna as a Director, and Jacob L. Barnhart as a Director of the Company on May 3, 2011.

Business of Citadel

We are an exploration company engaged in the exploration and development of oil and natural gas properties. Our property is located in the County of San Benito, California. Subject to availability of capital, we strive to implement an accelerated development program utilizing capital resources, a regional operating focus, an experienced management and technical team, and enhanced recovery technologies to attempt to increase production and increase returns for our stockholders. Our corporate strategy is to continue building value in the Company through successful exploration and development of gas and oil assets.

Our Property

On January 31, 2009, our wholly-owned subsidiary, Citadel Exploration, LLC (“CEL”), entered into an Oil and Gas Lease (“Lease”) for 688.71 acres of property with Vintage Petroleum, LLC (“Vintage”), a company owned by Occidental Petroleum (NYSE:OXY), for the purposes and with the exclusive right of prospecting, exploring, mining, drilling and operating the leased premises for oil and gas, and producing, taking, treating, storing oil only, removing and disposing of such substances from the leased premises, and Vintage grants to CEL all rights, privileges and easements useful or convenient for CEL’s operations to which Vintage has rights to lease on the leased premises, subject to the covenants, conditions and provisions of the lease agreement.

Pursuant to the Lease the primary term of the Lease is for three (3) years from January 31, 2009 and so long thereafter as any of the said substances is produced from the leased premises, or lands pooled therewith as allowed by the Lease, in paying quantities (that volume of production of oil or gas from a well which, when sold, is sufficient to yield a return to CEL in excess of the cost of operation of said well, measured by the average over a one hundred twenty day period), or so long as CEL shall conduct actual drilling operations or continue development (including, without limitation, drilling, re-drilling, deepening and reworking) or producing operations on the leased premises as provided by the Lease without cessation for more than one hundred twenty (120) consecutive days for wells that are drilled to a depth shallower than 12,500 feet below the surface of the earth or one hundred eighty (180) days for wells that are drilled to a depth greater than 12,500 feet below the surface of the earth. Actual drilling of a well shall be deemed to have commenced when a derrick, a rig, and machinery capable of drilling to a depth sufficient to test a prospective oil or gas horizon have been erected, and when such well has been spudded in and is rotating under power.

Rentals

Upon the execution of the Lease CEL paid Vintage the sum of \$20,661.30 (\$30/acre) as advance rental in full for a period ending January 31, 2010, one year from the date of the Lease.

If operations for actual drilling on the non active acreage are not commenced or have not occurred on said leased premises, or lands pooled therewith, on or before January 31, 2010 (1st anniversary date) the Lease shall then terminate, as to the non active acreage, by operation of law as to both parties unless on or before such anniversary date CEL shall pay to Vintage the sum of \$30.00 per non active acre which shall cover the privilege of deferring commencement of drilling operations on the non active acreage for a period of twelve (12) months. For the purposes of calculating rentals, non active acreage is any part of the leased premises not in a well unit or 640 acres for any drilling rig engaged in actual drilling activity on the leased premises on the anniversary date on which rentals are due. If operations for actual drilling on the non active acreage are not commenced or have not occurred on said leased premises, or lands pooled therewith, on or before January 31, 2011 (2nd anniversary date) the Lease shall then terminate, as to the non active acreage, by operation of law as to both parties unless on or before such anniversary date CEL shall pay to Vintage the sum of \$30.00 per non active acre (herein called “Rental”) which shall cover the privilege of deferring commencement of drilling operations on the non active acreage for a period of twelve (12) months.

Notwithstanding the above, if operation for actual drilling on the leased premises have commenced or have occurred on said leased premises, or lands pooled therewith, on or before January 31, 2010 (1st anniversary date) the Lease shall then terminate, as to the non active acreage, by operation of law as to both parties unless on or before each successive anniversary date CEL shall pay to Vintage the sum of \$30.00 per non active acre (herein called "Rental") which shall cover the privilege of deferring commencement of drilling operations on the non active acreage for a period of twelve (12) months.

During the primary term if (i) prior to the discovery of oil or gas on the leased premises or lands pooled therewith, CEL should drill a dry hole or holes on the leased premises or lands pooled therewith, or (ii) after the discovery of oil or gas the production thereof should cease for any cause, or (iii) a well on the leased premises or lands pooled therewith capable of producing gas in shut-in, the Lease shall not terminate if CEL (i) commences additional drilling or reworking operations within one hundred and twenty (120) or one hundred and fifty (150) days, and, (ii) if production ceases or shut-in occurs within one hundred twenty (120) or one hundred fifty days (150) days, thereafter, CEL pays Rental on or before the delay rental paying date next ensuing after the expiration of one hundred twenty (120) or one hundred and fifty (150) days from date of completion of a dry hole, the cessation of production, or the shutting-in of the gas well.

Royalties

On oil and other liquid hydrocarbons produced from each well located on the leased premises, the royalties shall be the market value of nineteen and one-half percent (19.5%) to be paid to Vintage and one-half of one percent (1/2 of 1%) to Pacific Minerals LLC (PML), a California limited liability company (pursuant to a non-executory royalty interest owned by PML) of that produced, saved or used from such well, the same to be delivered at such well or to the credit of Vintage, free of all costs of production or delivery into the pipeline to which the wells may be connected. If Vintage does not take such oil in kind, CEL shall market such oil at its market value, and the royalties payable shall be computed on such market value. If such oil is marketed by CEL, "market value" shall mean the proceeds received by CEL in an arms-length, good faith transaction with a third party purchaser, who is not a subsidiary or affiliate of CEL.

On gas, including casinghead gas or other gaseous substances, produced from each well located on the leased premises, the royalties shall be the market value of nineteen and one-half percent (19.5%) to Vintage and one-half percent (1/2 of 1%) to PML (pursuant to a non-executory royalty interest owned by PML) of the gas produced, used, vented or flared from such well (excepting any gas flared or vented during a reasonable test period), delivered to Vintage, free of all costs of production and delivery. Vintage may, with prior written consent, use, vent or flare, royalty free any gas produced from the well or wells located on the lease premises for operations conducted on the lease premises. If Vintage does not take such gas in kind, CEL shall market such gas at its market value, and the royalties payable shall be computed on such market value. With respect to gas sold by CEL the term "market value" shall mean the proceeds received by CEL in an arms-length, good faith transaction with a third party purchaser. If CEL sells gas in good faith to a third party who is not a subsidiary or an affiliate of CEL, and the gas is sold at a point off the leased premises, Vintage's royalty shall bear its pro rata share of reasonable transportation costs to such point of sale. Without the prior written consent of Vintage, CEL shall not (i) sell gas to any subsidiary or affiliate of CEL for transportation, gathering or treating of gas in a Hydrocarbon Recovery Plan, in the event transportation is chargeable against Vintage's interest, as provided for above.

In addition to the land owners' royalty, there is an overriding royalty of 2% that may be paid to the surface owner and a consulting geologic team.

Project Indian

Project Indian is located in the Bitterwater sub-basin of the Salinas Basin, north of the giant San Ardo Field. It is a shallow anticline defined by surface geology and well control that may have over 100 million barrels of heavy (11-14 gravity API) oil in place. A well that was drilled and cored extensively by Chevron in 1976 (Tannehill Ranch Corehole #9) showed the oil is trapped in highly porous and permeable basal Pliocene sands at 300-500 feet deep with 300' of claystone cap rock. This accumulation is a strong analog to another discovery made by the founders of CEL at Northwest San Ardo, albeit at a shallower depth.

We will develop Project Indian as a thermal recovery operation. The initial phase of evaluation will entail the drilling of 15 vertical wells in late 2011 and cyclic steaming to initiate production. Horizontal development may follow in 2012 following the analysis of steaming and production of vertical wells. Record high long term oil prices make a target of this size extremely attractive.

County of San Benito aerial photo of 688 acre mineral block defined by the red outline

Development Plan

The project will include the drilling of 15 wells to collect data on the subsurface reservoir. This data will be used to determine which wells are suitable candidates for a pilot thermal enhanced recovery program. Temporary equipment will be used to conduct a pilot thermal enhanced recovery program. The pilot recovery program will provide data that will help determine economic viability and potential future development of the subsurface reservoir. Highlights of this project include: 1) drilling and coring, 2) collecting and analyzing the data, 3) installation of temporary production facilities, 4) pilot steam injection and saturation, 5) well production test, and 6) collecting production and steam injection data and analyzing.

Upon successful completion of the pilot program testing we will begin the next phase of development. This includes installation of a natural gas utility line and electric power. We have already confirmed with Pacific Gas and Electric that utility gas and power are available within 2 miles of the project site. Temporary equipment will be utilized for initial operations and additional permanent equipment will be installed at a later date. All wells will then be placed in service and additional drilling will begin.

Oil and Natural Gas Industry Overview

Oil and natural gas prices are currently at high levels. Based on worldwide supply and demand projections and the potential for instability in areas that currently provide a large proportion of the world's petroleum, we believe that prices are likely to remain at high levels for the foreseeable future. We believe that this presents a tremendous opportunity for our Company to grow quickly. We have assembled an experienced and senior team of professionals to evaluate, acquire and manage available prospects. The experience of this team and its ability to quickly and accurately evaluate prospects and subsequently apply modern exploration, development and production techniques should be key to our company's success. A number of factors, including high product prices, the ease and availability of capital, and the influx of that capital into the oil and natural gas sector has resulted in tremendous competition for prospects, people, equipment and services in recent years. We believe that our planned ability to quickly and accurately assess opportunities worth pursuing, to negotiate the best possible terms and to attract the people, equipment and services required to finance and effect the projects should constitute a competitive advantage. Our goal is to grow our Company and increase stockholder value in a favorable petroleum pricing environment. We believe a focus on oil and gas will result in success and growth through added reserves and cash flow which will, in turn, provide a base for further growth and increases in stockholder value.

Our Business Strategy

Our principal strategy has been to focus on the acquisition and drilling of prospective oil and natural gas mineral leases. Once we have tested a prospect as productive, subject to availability of capital, we will implement a development program with a regional operating focus in order to increase production and increase returns for our stockholders. Exploration, acquisition and development activities are currently focused in California. Depending on availability of capital, and other constraints, our goal is to increase stockholder value by finding and developing oil and natural gas reserves at costs that provide an attractive rate of return on our investments. The principal elements of our business strategy are:

- **Develop Our Existing Property.** We intend to create reserve and production growth from our drilling locations we have identified on our property. The expected ultimate recovery and production rates of our properties, are anticipated to yield long-term profitability.
- **Maximize Operational Control.** We seek to operate our properties and maintain a substantial working interest. We believe the ability to control our drilling inventory will provide us with the opportunity to more efficiently allocate capital, manage resources, control operating and development costs, and utilize our experience and knowledge of oilfield technologies.
- **Pursue Selective Acquisitions and Joint Ventures.** We believe we are well-positioned to pursue selected acquisitions, subject to availability of capital, from the fragmented and capital-constrained owners of mineral rights throughout California.
- **Reduce Unit Costs Through Economies of Scale and Efficient Operations.** As we increase our oil production and develop our existing property, we expect that our unit cost structure will benefit from economies of scale. In particular, we anticipate reducing unit costs by greater utilization of our existing infrastructure over a larger number of wells.

We are continually evaluating oil and natural gas opportunities in California and are also in various stages of discussions with potential joint venture (“JV”) partners who may contribute capital to develop leases we currently own or would acquire for the JV. This economic strategy is anticipated to allow us to utilize our own financial assets toward the growth of our leased acreage holdings, pursue the acquisition of strategic oil and natural gas producing properties or companies and generally expand our existing operations while further diversifying risk. Subject to availability of capital, we plan to continue to bring potential acquisition and JV opportunities to various financial partners for evaluation and funding options.

Our future financial results will continue to depend on: (i) our ability to source and screen potential projects; (ii) our ability to discover commercial quantities of natural gas and oil; (iii) the market price for oil and natural gas; and (iv) our ability to fully implement our exploration, work-over and development program, which is in part dependent on the availability of capital resources. There can be no assurance that we will be successful in any of these respects, that the prices of oil and natural gas prevailing at the time of production will be at a level allowing for profitable production, or that we will be able to obtain additional funding at terms favorable to us to increase our currently limited capital resources. For a detailed description of these and other factors that could materially impact actual results, please see “Risk Factors” in this report.

Glossary of Terms

Term	Definition
API Gravity	Is a measure of how heavy or light a petroleum liquid is compared to water. If its API gravity is greater than 10, it is lighter and floats on water; if less than 10, it is heavier and sinks.
Barrel	In the energy industry, a barrel is a unit of volume measurement used for petroleum and is equivalent to 42 U.S. gallons measured at 60 ° Fahrenheit.
Basin	A depressed area where sediments have accumulated during geologic time and considered to be prospective for oil and gas deposits.
Blowout	An uncontrolled flow of oil, gas, water or mud from a wellbore caused when drilling activity penetrates a rock layer with natural pressures greater than the drilling mud in the borehole.
Completion / Completing	A well made ready to produce oil or natural gas. Completion involves cleaning out the well, running and cementing steel casing in the hole, adding permanent surface control equipment, and perforating the casing so oil or gas can flow into the well and be brought to the surface.
Desorb	The release of materials (e.g., gas molecules) from being adsorbed onto a surface. The opposite of adsorb.
Development	The phase in which a proven oil or gas field is brought into production by drilling production (development) wells.
Division order	A contract for the sale of oil or gas, by the holder of a revenue interest in a well or property, to the purchaser (often a pipeline transmission company).
Drilling	The using of a rig and crew for the drilling, suspension, production testing, capping, plugging and abandoning, deepening, plugging back, sidetracking, re-drilling or reconditioning of a well. Contrast to "Completion" definition.
Drilling logs	Recorded observations made of rock chips cut from the formation by the drill bit, and brought to the surface with the mud, as well as rate of penetration of the drill bit through rock formations. Used by geologists to obtain formation data.
Exploration	The phase of operations which covers the search for oil or gas by carrying out detailed geological and geophysical surveys followed up where appropriate by exploratory drilling. Compare to "Development" phase.
Farm out	Assignment or partial assignment of an oil and gas lease from one lessee to another lessee

Gathering line / system	A pipeline that transports oil or gas from a central point of production to a transmission line or mainline.
Gross acre	An acre in which a working interest is owned. The number of gross acres is the total number of acres in which a working interest is owned
Gross well	A well in which a working interest is owned. The number of gross wells is the total number of wells in which a working interest is owned.
Held-By-Production (HBP)	Refers to an oil and gas property under lease, in which the lease continues to be in force, because of production from the property.
Land services	Services performed by an oil and gas company or agent, or landman, who negotiates oil and gas leases with mineral owners, cures title defects, and negotiates with other companies on agreements concerning the lease.
Logging (electric logging)	Process of lowering sensors into a wellbore to acquire downhole recordings that indicate a well's rock formation characteristics and indications of hydrocarbons
Methane	An organic chemical compound of hydrogen and carbon (i.e., hydrocarbon), with the simplest molecular structure (CH ₄)
Mineral Lease	A legal instrument executed by a mineral owner granting exclusive right to another to explore, drill, and produce oil and gas from a piece of land
Natural gas quality	The value of natural gas is calculated by its BTU content. A cubic foot of natural gas on the average gives off 1000 BTU, but the range of values is between 500 and 1500 BTU. Energy content of natural gas is variable and depends on its accumulations which are influenced by the amount and types of energy gases they contain: the more non-combustible gases in a natural gas, the lower the Btu value.
Net acre	A net acre is deemed to exist when the sum of fractional working interests owned in gross acres equals one. The number of net acres is the sum of fractional working interests owned in gross acres expressed as whole numbers and fractions thereof.
Net well	A net well is deemed to exist when the sum of fractional working interests owned in gross wells equals one. The number of net wells is the sum of fractional working interests owned in gross wells expressed as whole numbers and fractions thereof.
Operator	A person, acting for himself or as an agent for others and designated to the state authorities as the one who has the primary responsibility for complying with its rules and regulations in any and all acts subject to the jurisdiction of the state
Permeability	

The property of a rock formation which quantifies the flow of a fluid through the pore spaces and into the wellbore.

Pooled, Pooled Unit A term frequently used interchangeably with "Unitization" but more properly used to denominate the bringing together of small tracts sufficient for the granting of a well permit under applicable spacing rules.

Proved Reserves	<p>Estimated quantities of crude oil, natural gas, condensate, or other hydrocarbons that geological and engineering data demonstrate with reasonable certainty to be commercially recoverable in the future from known reservoirs under existing conditions using established operating procedures and under current governmental regulations.</p> <p>Further definitions of oil and gas reserves, as defined by the SEC, can be found in Rule 4-10(a)(2)(i)-(iii) and Rule 4-10(a)(3) and (4). These Rules are available at the SEC's website; http://www.sec.gov/divisions/corpfin/forms/regsx.htm#gas</p>
Re-completion	Completion of an existing well for production from one formation or reservoir to another formation or reservoir that exists behind casing of the same well.
Reserves	Generally the amount of oil or gas in a particular reservoir that is available for production.
Reservoir	The underground rock formation where oil and gas has accumulated. It consists of a porous rock to hold the oil or gas, and a cap rock that prevents its escape
Reservoir Pressure	The pressure at the face of the producing formation when the well is shut-in. It equals the shut in pressure at the wellhead plus the weight of the column of oil in the hole.
Shut-in well	A well which is capable of producing but is not presently producing. Reasons for a well being shut-in may be lack of equipment, market or other.
Stratigraphic Trap	A variety of sealed geologic containers capable of retaining hydrocarbons, formed by changes in rock type or pinch-outs, unconformities, or sedimentary features.
Structural Trap	A variety of sealed geologic structures capable of retaining hydrocarbons, such as a faults or a folds.
Undeveloped acreage	Leased acreage which has yet to be drilled on to test the potential for hydrocarbons.
Unitize, Unitization	Joint operations to maximize produced hydrocarbon recovery among separate operators within a common reservoir
Working Interest	The right granted to the lessee of a property to explore for and to produce and own oil, gas, or other minerals. The working interest owners bear the exploration, development, and operating costs on either a cash, penalty, or carried basis.

Competition

The oil and natural gas industry is intensely competitive. We compete with numerous individuals and companies, including many major oil and natural gas companies, which have substantially greater technical, financial and operational resources and staff. Accordingly, there is a high degree of competition for desirable oil and natural gas leases, suitable properties for drilling operations and necessary drilling equipment, as well as for access to funds.

Governmental Regulations

Regulation of Oil and Natural Gas Production. Our oil and natural gas exploration, production and related operations, when developed, are subject to extensive rules and regulations promulgated by federal, state, tribal and local authorities and agencies. For example, some states in which we may operate, including California, require permits for drilling operations, drilling bonds and reports concerning operations and impose other requirements relating to the exploration and production of oil and natural gas. Such states may also have statutes or regulations addressing conservation matters, including provisions for the unitization or pooling of oil and natural gas properties, the establishment of maximum rates of production from wells, and the regulation of spacing, plugging and abandonment of such wells. Failure to comply with any such rules and regulations can result in substantial penalties. Moreover, such states may place burdens from previous operations on current lease owners, and the burdens could be significant. The regulatory burden on the oil and natural gas industry will most likely increase our cost of doing business and may affect our profitability. Although we believe we are currently in substantial compliance with all applicable laws and regulations, because such rules and regulations are frequently amended or reinterpreted, we are unable to predict the future cost or impact of complying with such laws. Significant expenditures may be required to comply with governmental laws and regulations and may have a material adverse effect on our financial condition and results of operations.

Federal Regulation of Natural Gas. The Federal Energy Regulatory Commission (“FERC”) regulates interstate natural gas transportation rates and service conditions, which may affect the marketing of natural gas produced by us, as well as the revenues that may be received by us for sales of such production. Since the mid-1980’s, FERC has issued a series of orders, culminating in Order Nos. 636, 636-A and 636-B (“Order 636”), that have significantly altered the marketing and transportation of natural gas. Order 636 mandated a fundamental restructuring of interstate pipeline sales and transportation service, including the unbundling by interstate pipelines of the sale, transportation, storage and other components of the city-gate sales services such pipelines previously performed. One of FERC’s purposes in issuing the order was to increase competition within all phases of the natural gas industry. The United States Court of Appeals for the District of Columbia Circuit largely upheld Order 636 and the Supreme Court has declined to hear the appeal from that decision. Generally, Order 636 has eliminated or substantially reduced the interstate pipelines’ traditional role as wholesalers of natural gas in favor of providing only storage and transportation service, and has substantially increased competition and volatility in natural gas markets.

The price we may receive from the sale of oil and natural gas liquids will be affected by the cost of transporting products to markets. Effective September 28, 1995, FERC implemented regulations establishing an indexing system for transportation rates for oil pipelines, which, generally, would index such rates to inflation, subject to certain conditions and limitations. We are not able to predict with certainty the effect, if any, of these regulations on our intended operations. However, the regulations may increase transportation costs or reduce well head prices for oil and natural gas liquids.

Environmental Matters

Our operations and properties are subject to extensive and changing federal, state and local laws and regulations relating to environmental protection, including the generation, storage, handling, emission, transportation and discharge of materials into the environment, and relating to safety and health. The recent trend in environmental legislation and regulation generally is toward stricter standards, and this trend will likely continue.

These laws and regulations may:

- require the acquisition of a permit or other authorization before construction or drilling commences and for certain other activities;
- limit or prohibit construction, drilling and other activities on certain lands lying within wilderness and other protected areas; and
- impose substantial liabilities for pollution resulting from its operations, or due to previous operations conducted on any leased lands.

The permits required for our operations may be subject to revocation, modification and renewal by issuing authorities. Governmental authorities have the power to enforce their regulations, and violations are subject to fines or injunctions, or both. In the opinion of management, we are in substantial compliance with current applicable environmental laws and regulations, and have no material commitments for capital expenditures to comply with existing environmental requirements. Nevertheless, changes in existing environmental laws and regulations or in interpretations thereof could have a significant impact on us, as well as the oil and natural gas industry in general.

The Comprehensive Environmental, Response, Compensation, and Liability Act, as amended (“CERCLA”), and comparable state statutes impose strict, joint and several liability on owners and operators of sites and on persons who disposed of or arranged for the disposal of “hazardous substances” found at such sites. It is not uncommon for the neighboring land owners and other third parties to file claims for personal injury and property damage allegedly caused by the hazardous substances released into the environment. The Federal Resource Conservation and Recovery Act, as amended (“RCRA”), and comparable state statutes govern the disposal of “solid waste” and “hazardous waste” and authorize the imposition of substantial fines and penalties for noncompliance. Although CERCLA currently excludes petroleum from its definition of “hazardous substance,” state laws affecting our operations may impose clean-up liability relating to petroleum and petroleum related products. In addition, although RCRA classifies certain oil field wastes as “non-hazardous,” such exploration and production wastes could be reclassified as hazardous wastes thereby making such wastes subject to more stringent handling and disposal requirements.

The Federal Water Pollution Control Act of 1972, as amended (“Clean Water Act”), and analogous state laws impose restrictions and controls on the discharge of pollutants into federal and state waters. These laws also regulate the discharge of storm water in process areas. Pursuant to these laws and regulations, we are required to obtain and maintain approvals or permits for the discharge of wastewater and storm water and develop and implement spill prevention, control and countermeasure plans, also referred to as “SPCC plans,” in connection with on-site storage of greater than threshold quantities of oil. The EPA issued revised SPCC rules in July 2002 whereby SPCC plans are subject to more rigorous review and certification procedures. We believe that our operations are in substantial compliance with applicable Clean Water Act and analogous state requirements, including those relating to wastewater and storm water discharges and SPCC plans.

The Endangered Species Act, as amended (“ESA”), seeks to ensure that activities do not jeopardize endangered or threatened animal, fish and plant species, nor destroy or modify the critical habitat of such species. Under ESA, exploration and production operations, as well as actions by federal agencies, may not significantly impair or jeopardize the species or its habitat. ESA provides for criminal penalties for willful violations of the Act. Other statutes that provide protection to animal and plant species and that may apply to our operations include, but are not necessarily limited to, the Fish and Wildlife Coordination Act, the Fishery Conservation and Management Act, the Migratory Bird Treaty Act and the National Historic Preservation Act. Although we believe that our operations will be in substantial compliance with such statutes, any change in these statutes or any reclassification of a species as endangered could subject us to significant expenses to modify our operations or could force us to discontinue certain operations altogether.

Personnel

As of the date of this report, and as a result of our recent organizational establishment, we had no full-time employees. As production and drilling activities increase or decrease, we may have to adjust our technical, operational and administrative personnel as appropriate. We are using and will continue to use independent consultants and contractors to perform various professional services, particularly in the area of land services, reservoir engineering, geology drilling, water hauling, pipeline construction, well design, well-site monitoring and surveillance, permitting and environmental assessment. We believe that this use of third-party service providers may enhance our ability to contain operating and general expenses, and capital costs.

RISK FACTORS

An investment in our common stock involves a high degree of risk. You should carefully consider the risks described below, together with all of the other information included in this report, before making an investment decision. If any of the following risks actually occurs, our business, financial condition or results of operations could suffer. In that case, the trading price of our common stock could decline, and you may lose all or part of your investment. You should read the section entitled “Special Note Regarding Forward Looking Statements” above for a discussion of what types of statements are forward-looking statements, as well as the significance of such statements in the context of this report.

RISKS ASSOCIATED WITH OIL AND GAS OPERATIONS

Drilling wells is speculative, often involving significant costs that may be more than our estimates, and may not result in any addition to our production or reserves. Any material inaccuracies in drilling costs, estimates or underlying assumptions will materially affect our business.

Developing and exploring for natural gas and oil involves a high degree of operational and financial risk, which precludes definitive statements as to the time required and costs involved in reaching certain objectives. The budgeted costs of drilling, completing and operating wells are often exceeded and can increase significantly when drilling costs rise due to a tightening in the supply of various types of oilfield equipment and related services. Drilling may be unsuccessful for many reasons, including title problems, weather, cost overruns, equipment shortages and mechanical difficulties. Moreover, the successful drilling of a natural gas or oil well does not ensure a profit on investment. Exploratory wells bear a much greater risk of loss than development wells. A variety of factors, both geological and market-related, can cause a well to become uneconomical or only marginally economic. Our initial drilling and development sites, and any potential additional sites that may be developed, require significant additional exploration and development, regulatory approval and commitments of resources prior to commercial development. Any success that we may have with these wells or any future drilling operations will most likely not be indicative of our current or future drilling success rate, particularly, because we intend to emphasize on exploratory drilling. If our actual drilling and development costs are significantly more than our estimated costs, we may not be able to continue our business operations as proposed and would be forced to modify our plan of operation.

Development of our reserves, when established, may not occur as scheduled and the actual results may not be as anticipated. Drilling activity may result in downward adjustments in reserves or higher than anticipated costs. Our estimates will be based on various assumptions, including assumptions required by the Securities and Exchange Commission relating to natural gas and oil prices, drilling and operating expenses, capital expenditures, taxes and availability of funds. The process of estimating our natural gas and oil reserves is anticipated to be extremely complex, and will require significant decisions and assumptions in the evaluation of available geological, geophysical, engineering and economic data for each reservoir. Due to our inexperience in the oil and gas industry, our estimates may not be reliable enough to allow us to be successful in our intended business operations. Our actual production, revenues, taxes, development expenditures and operating expenses will likely vary from those anticipated. These variances may be material.

If we are unable to continue drilling operations pursuant to the terms set forth in our lease agreement with Vintage Petroleum, LLC, the lease agreement may be terminated. If we were to lose the lease our financial condition and results of operations would be adversely affected.

Our lease ownership is subject to termination in the event we are unable to continue drilling operations as set forth in the lease agreement. In the event we are unable to continue with our drilling operations, then we will lose our rights to the lease. Such loss would prevent us from pursuing development activity on the leased property and will have a substantial impact on our financial condition and results of operations.

Gas and Oil prices are volatile. This volatility may occur in the future, causing negative change in cash flows which may result in our inability to cover our capital expenditures.