

CROFF ENTERPRISES INC  
Form 10-Q  
November 09, 2006

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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

WASHINGTON, D.C. 20549

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**FORM 10-Q**

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

For the Quarterly and nine month Period Ended September 30, 2006

OR

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

For the Transition Period From            to

Commission File Number: 000-16731

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**CROFF ENTERPRISES, INC.**

(Exact name of registrant as specified in its charter)

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**Utah**  
(State or other jurisdiction of incorporation or organization)

**87-0233535**  
(I.R.S. Employer Identification No.)

**3773 Cherry Creek Drive North, Suite 1025**  
**Denver, Colorado**  
(Address of principal executive office)

**80209**  
(Zip Code)  
**(303)-383-1555**

**Securities registered pursuant to Section 12(b) of the Act:**  
**Common - \$0.10 Par Value**

**Name of each exchange on which registered:**  
**None**

**Securities registered pursuant to Section 12(g) of the Act: None**

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Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.  Yes  No

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act).  Yes  No

There were 551,244 shares of common stock outstanding on October 31, 2006, exclusive of 69,399 common shares held as treasury stock.

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**CROFF ENTERPRISES, INC.**

**FORM 10-Q**

**For the Quarter and Nine Months ended Ended September 30, 2006 (UNAUDITED)**

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**Forward-Looking Statements**

Certain information included in this report, other materials filed or to be filed by the Company with the Securities and Exchange Commission ("SEC"), as well as information included in oral statements or other written statements made or to be made by the Company contain or incorporate by reference certain forward looking statements (other than statements of historical or present fact) within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934.

All statements, other than statements of historical or present facts, that address activities, events, outcomes or developments that the Company plans, expects, believes, assumes, budgets, predicts, forecasts, estimates, projects, intends or anticipates (and other similar expressions) will or may occur in the future are forward looking statements. These forward-looking statements are based on management's current belief, based on currently available information, as to the outcome and timing of future events. When considering forward-looking statements, you should keep in

mind the cautionary statements in this Form 10-Q and the Company's Annual Report on Form 10-K for the year ended December 31, 2005. Such forward-looking statements appear in a number of places and include statements with respect to, among other things, such matters as: future capital, development and exploration expenditures (including the amount and nature thereof), drilling, deepening or refracing of wells, oil and natural gas reserve estimates (including estimates of future net revenues associated with such reserves and the present value of such future net revenues), estimates of future production of oil and natural gas, business strategies, expansion and growth of the Company's operations, cash flow and anticipated liquidity, prospects and development and property acquisitions, obtaining financial or industry partners for prospect or program development, or marketing of oil and natural gas. We caution you that these forward-looking statements are subject to risks and uncertainties.

These risks include but are not limited to: general economic conditions, the Company's ability to finance acquisitions and drilling, the market price of oil and natural gas, the risks associated with exploration, the Company's ability to find, acquire, market, develop and produce new properties, operating hazards attendant to the oil and natural gas business, uncertainties in the estimation of proved reserves and in the projection of future rates of production and timing of development expenditures, the strength and financial resources of the Company's competitors, the Company's ability to find and retain skilled personnel, climatic conditions, labor relations, availability and cost of material and equipment, environmental risks, the results of financing efforts, regulatory developments and the other risks described in the Company's Annual Report on Form 10-K for the year ended December 31, 2005.

Reserve engineering is a subjective process of estimating underground accumulations of oil and natural gas that cannot be measured in an exact way. The accuracy of any reserve estimate depends on the quality of available data and the interpretation of that data by reserve engineers. In addition, the results of drilling, testing and production activities may justify revisions of estimates that were made previously. If significant, these revisions could change the schedule of any further production and/or development drilling. Accordingly, reserve estimates are generally different from the quantities of oil and natural gas that are ultimately recovered.

Should one or more of the risks or uncertainties described above or elsewhere in this Form 10-Q or presented in the Company's Annual Report on Form 10-K for the year ended December 31, 2005 occur, or should underlying assumptions prove incorrect, actual results and plans could differ materially from those expressed in any forward-looking statements. We specifically disclaim all responsibility to publicly update any information contained in a forward-looking statement or any forward-looking statement in its entirety and therefore disclaim any resulting liability for potentially related damages.

All forward-looking statements attributable to us are expressly qualified in their entirety by this cautionary statement.

## **Part I. Unaudited Financial Information**

### **ITEM 1. Unaudited Financial Statements**

The financial statements included herein have been prepared in conformity with generally accepted accounting principles. The statements are unaudited but reflect all adjustments, which, in the opinion of management, are necessary to fairly present the Company's financial position and results of operations. All such adjustments are of a normal recurring nature.

## CROFF ENTERPRISES, INC. BALANCE SHEETS (Unaudited)

|   | December 31,<br>2005 | September 30,<br>2006 |
|---|----------------------|-----------------------|
| <b>ASSETS:</b>  |                      |                       |
| Current Assets:   |                      |                       |
| Cash and cash equivalents   | \$ 902,257           | \$ 1,018,560          |
| Accounts receivable   | 157,959              | 131,855               |
|   | <u>1,060,216</u>     | <u>1,150,415</u>      |
| Oil and natural gas properties, at cost, successful efforts method:   | 1,282,616            | 1,294,500             |
| Accumulated depletion and depreciation  | (535,330)            | (571,830)             |
|   | <u>747,286</u>       | <u>722,670</u>        |
| <b>Total Assets:</b>  | <b>\$ 1,807,502</b>  | <b>\$ 1,873,085</b>   |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>   |                      |                       |
| Current Liabilities:  |                      |                       |
| Accounts payable  | \$ 37,945            | \$ 87,886             |
| Farmout agreement liability   | 300,621              | --                    |
| Current portion of ARO liability  | 23,000               | 23,000                |
| Accrued liabilities   | 72,788               | 93,375                |
|   | <u>434,354</u>       | <u>204,261</u>        |
| Long-term portion of ARO liability  | <u>58,828</u>        | <u>\$ 63,228</u>      |
| Stockholders' equity:   |                      |                       |
| Class A Preferred stock, no par value<br>5,000,000 shares authorized, none issued                           | --                   | --                    |
| Class B Preferred stock, no par value<br>1,000,000 shares authorized, 540,659 shares issued and outstanding | 1,089,233            | 1,296,682             |
| Common stock, \$.10 par value<br>20,000,000 shares authorized, 620,643 shares issued and outstanding        | 62,064               | 62,064                |
| Capital in excess of par value  | 155,715              | 155,715               |
| Treasury stock, at cost, 69,399<br>issued and outstanding in 2005 and 2006                                  | (107,794)            | (107,794)             |
| Retained earnings   | 115,102              | 198,929               |
|   | <u>1,314,320</u>     | <u>1,605,596</u>      |
| <b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>   | <b>\$ 1,807,502</b>  | <b>\$ 1,873,085</b>   |

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See accompanying notes to unaudited condensed financial statements.

## CROFF ENTERPRISES, INC.

## STATEMENT OF OPERATIONS

(Unaudited)

|  | Three Months Ended<br>September 30 |                   | Nine Months Ended<br>September 30 |                   |
|--|------------------------------------|-------------------|-----------------------------------|-------------------|
|  | 2005                               | 2006              | 2005                              | 2006              |
| <b>Revenues:</b>                                     |                                    |                   |                                   |                   |
| Oil and natural gas sales                            | \$ 247,288                         | \$ 231,180        | \$ 627,274                        | \$ 666,286        |
| Interest income                                      | --                                 | 24,657            | --                                | 38,536            |
| Other income   | 7,059                              | --                | 25,669                            | --                |
| Gain on Sale of Asset                                | --                                 | 112,543           | --                                | 112,543           |
|  | <u>254,347</u>                     | <u>368,380</u>    | <u>652,943</u>                    | <u>817,365</u>    |
| <b>Expenses:</b>                                     |                                    |                   |                                   |                   |
| Lease operating expense including production taxes   | 46,253                             | 73,394            | 209,016                           | 196,552           |
| General and administrative                           | 35,327                             | 36,346            | 105,105                           | 135,172           |
| Overhead expense, related party                      | 11,674                             | 19,020            | 36,371                            | 43,464            |
| Accretion expense                                    | 7,640                              | 1,467             | 7,640                             | 4,401             |
| Depletion and depreciation                           | 12,000                             | 12,000            | 33,000                            | 36,500            |
|  | <u>112,894</u>                     | <u>142,227</u>    | <u>410,132</u>                    | <u>416,089</u>    |
| Pretax income (loss)                                 | 141,453                            | 226,153           | 242,811                           | 401,276           |
| Provision for income taxes:                          | 29,690                             | 72,000            | 45,540                            | 110,000           |
| Net income (loss)                                    | <u>\$ 111,763</u>                  | <u>\$ 154,153</u> | <u>\$ 197,271</u>                 | <u>\$ 291,276</u> |
| Net income applicable to preferred B shares:         | <u>95,551</u>                      | <u>75,358</u>     | <u>216,692</u>                    | <u>207,449</u>    |
| Net income (loss) applicable to common shares        | <u>\$ 16,212</u>                   | <u>\$ 78,795</u>  | <u>\$ (19,421)</u>                | <u>\$ 83,827</u>  |
| Basic and diluted net income (loss) per common share | <u>\$ 0.03</u>                     | <u>\$ 0.14</u>    | <u>\$ (0.03)</u>                  | <u>\$ 0.15</u>    |



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|  |         |         |         |         |
|--|---------|---------|---------|---------|
| Weighted average common shares outstanding | 567,400 | 551,244 | 567,400 | 551,244 |
|--|---------|---------|---------|---------|

\* less than \$0.01 per share

See accompanying notes to unaudited condensed financial statements.

**CROFF ENTERPRISES, INC.**  
**STATEMENTS OF STOCKHOLDERS' EQUITY**  
For the year ended December 31, 2005 and the nine months ended September 30, 2006  
(Unaudited)

|   | Preferred B stock |                    | Common stock   |                  | Capital<br>in<br>Excess<br>of<br>Par<br>Value | Treasury<br>stock | Accumulated<br>Earnings |
|---|-------------------|--------------------|----------------|------------------|---|-------------------|-------------------------|
|   | <u>Shares</u>     | <u>Amount</u>      | <u>Shares</u>  | <u>Amount</u>    | <u>Value</u>                                  | <u>stock</u>      | <u>Earnings</u>         |
| Balance at December 31, 2005                            | 540,659           | \$1,089,233        | 620,643        | \$ 62,064        | \$155,715                                     | \$ (107,794)      | \$ 115,102              |
| Net income for the nine months ended September 30, 2006 | --                | --                 | --             | --               | --  | --                | 291,276                 |
| Preferred Stock reallocation                            | --                | 207,449            | --             | --               | --  | --                | (207,449)               |
| <b>Balance at September 30, 2006</b>                    | <b>540,659</b>    | <b>\$1,296,682</b> | <b>620,643</b> | <b>\$ 62,064</b> | <b>\$ 155,715</b>                             | <b>(107,794)</b>  | <b>\$ 198,929</b>       |

See accompanying notes to unaudited condensed financial statements.

## CROFF ENTERPRISES, INC.

## STATEMENT OF CASH FLOWS

For the nine months ended September 30, 2005 and 2006

(Unaudited)

|   | <u>2005</u>              | <u>2006</u>                |
|---|--------------------------|----------------------------|
| <b>Cash flows from operating activities:</b>                                      |                          |                            |
| Net income  | \$ 197,271               | \$ 291,449                 |
| Adjustments to reconcile net income to net cash provided by operating activities: |                          |                            |
| Depletion, depreciation, and accretion  | 40,640                   | 40,901                     |
| Loss on Abandonment   | 56,089                   | --                         |
| Gain on sale of assets  | (14,173)                 | (112,543)                  |
| Changes in operating assets and liabilities:                                      |                          |                            |
| Accounts receivable   | (44,892)                 | 26,104                     |
| Accounts payable  | 2,607                    | 49,941                     |
| Accrued liabilities   | 37,078                   | 20,587                     |
| <b>Net cash provided by operating activities</b>                                  | <b><u>274,620</u></b>    | <b><u>316,439</u></b>      |
| <b>Cash flows from investing activities:</b>                                      |                          |                            |
| Proceeds from sale of assets  | 48,500                   | 210,550                    |
| Acquisition of property leases and improvements                                   | (57,194)                 | (110,065)                  |
| <b>Net cash provided in investing activities</b>                                  | <b><u>(8,694)</u></b>    | <b><u>100,485</u></b>      |
| <b>Cash flows from investment activities:</b>                                     |                          |                            |
| Costs incurred for the benefit of farmout agreement                               | --                       | (300,621)                  |
| <b>Net cash (used) by financing activities</b>                                    | <b><u>--</u></b>         | <b><u>(300,621)</u></b>    |
| Net increase (decrease) in cash and cash equivalents                              | 265,926                  | 116,303                    |
| Cash and cash equivalents at beginning of period                                  | 257,667                  | 902,257                    |
| <b>Cash and cash equivalents at end of period</b>                                 | <b><u>\$ 523,593</u></b> | <b><u>\$ 1,018,560</u></b> |

Supplemental disclosure of non-cash investing and financing activities:

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During the nine month period end September 30, 2005, the Company purchased 1,500 shares of its common stock for \$2,362 now included in the treasury.

See accompanying notes to unaudited condensed financial statements.

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**CROFF ENTERPRISES, INC**

**NOTES TO UNAUDITED CONDENSED FINANCIAL STATEMENTS**

**Basis of Preparation**

The condensed financial statements for the three and nine month periods ended September 30, 2005 and 2006 in this report have been prepared by the Company without audit pursuant to the rules and regulations of the Securities and Exchange Commission and reflect, in the opinion of the management, all adjustments necessary to present fairly the results of the operations of the interim periods presented herein. Certain information in footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been omitted pursuant to such rules and regulations, although the Company believes the disclosures presented herein are adequate to make the information presented not misleading. It is suggested that these condensed financial statements be read in conjunction with the financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2005, which report has been filed with the Securities and Exchange Commission. The Annual Report is available from the Company's website at [www.croff.com](http://www.croff.com), and online at the Securities and Exchange Commission website at [www.sec.gov/edgar](http://www.sec.gov/edgar).

**ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

Overview

Croff Enterprises, Inc. ("Croff" or the "Company") was incorporated in Utah in 1907. Croff is an independent energy company engaged in the business of oil and natural gas exploration and production, primarily through the acquisition of producing oil and natural gas leases as well as the ownership of perpetual mineral interests. Other companies operate almost all of the wells from which Croff receives revenues and Croff has no control over the factors which determine royalty or working interest revenues, such as markets, prices and rates of production. Today, Croff participates as a working interest owner in approximately 40 wells or units of several wells. Croff holds small royalty interests in approximately 212 wells.

Croff's business strategy is focused on targeting opportunities that are of lower risk with the potential for stable cash flow and long asset life while seeking to keep operating costs low. The Company has no short-term or long-term debt outstanding. Over the last six years, the Company acquired an interest in three wells in Michigan, one well in Montana, six wells in Oklahoma and nine wells in Texas. In 2006 the Company has a small working interest in three wells being drilled in Wyoming and one being drilled in Utah. In 2004, the Company sold its Yorktown Re-entry Program to Tempest Energy Resources LP, retaining a 25% interest in the Area of Mutual Interest (AMI). The first re-entry well in this program was unsuccessful, and Tempest declined to participate in the balance of the acreage. In June, 2006, the Company reached an agreement to sell all of its assets in the Yorktown Program except a working interest in two wells. The sale was for approximately the Company's cost in the program. Since the Company had written off part of its costs in 2005, the sale resulted in a gain reported in the third quarter of 2006.

During the last 12 months, the Company has been involved in seeking strategic alternatives to its previous business. On April 8, 2005, the Company announced that it would seek such strategic alternatives to attempt to enhance shareholder value and liquidity. Beginning in June and completed in August 2005, shareholders received a tender offer for their Preferred B shares from private companies owned by the Company's President and Chairman. Following the tender offer, the President and his affiliated companies own approximately 67% of the outstanding Preferred B shares of the Company. The Company continues to engage in negotiations intended to create more value and liquidity for its shareholders, which may result in the change of control and business of the Company. There is no assurance these negotiations will be successful.

#### Critical Accounting Policies and Estimates

The Company's discussion and analysis of its financial condition and results of operation are based upon financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires the Company to make estimates and judgments that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the year. The Company analyzes its estimates, including those related to oil and natural gas revenues, oil and natural gas properties, marketable securities, income taxes and contingencies.

The Company bases its estimates on historical experience and various other assumptions that are believed to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions. The Company believes the following critical accounting policies affect its more significant judgments and estimates used in the preparation of its financial statements and the uncertainties that it could impact results of operations, financial conditions and cash flows. The Company accounts for its oil and natural gas properties under the successful efforts method of accounting. Depletion, depreciation and amortization of oil and natural gas properties and the periodic assessments for impairment are based on underlying oil and natural gas reserve estimates and future cash flows using then current oil and natural gas prices combined with operating and capital development costs. There are numerous uncertainties inherent in estimating quantities of proved oil and natural gas reserves and in projecting future rates of production and timing of development expenditures. Historically, oil and natural gas prices have experienced significant fluctuations and have been particularly volatile in recent years. Price fluctuations can result from variations in weather, levels of regional or national production and demand, availability of transportation capacity to other regions of the country and various other factors. Increases or decreases in oil and natural gas prices received could have a significant impact on future results.

## Liquidity and Capital Resources

At September 30, 2006, the Company had assets of \$1,873,085 and current assets totaled \$1,150,415 compared to current liabilities of \$204,261. The Company's current assets are the combinations of cash and cash equivalents and accounts receivable and the Company's current liabilities are a combination of accounts payable, asset recovery liability and accrued liabilities such as provision for income taxes. Working capital at September 30, 2006 totaled \$946,154, an increase of 51% compared to \$625,862 at December 31, 2005. The Company had a current ratio at September 30, 2006 of approximately 5:1. During the nine month period ended September 30, 2006, net cash provided by operations totaled \$316,439, as compared to \$274,620 for the same period in 2005. This increase was due to the gain on sale of the Panther Pipeline and the Edwards Dixel Gips lease in Dewitt County, Texas in 2006, and the write-off of a portion of the Dewitt County assets in 2005. The cost basis for the Panther pipeline was \$40,000 and the cost basis in the Edwards Dixel Gips lease was \$102,459, for a total of \$142,459. The proceeds from the sale were \$255,000 yielding a gross gain for this transaction of \$112,543. The Company had no short-term or long-term debt outstanding at September 30, 2006. In December, 2005, the Company purchased 16,156 shares of its common stock at a cost of \$24,643, which is included in the treasury at September 30, 2006.

The Company's plans for ongoing development, acquisition and exploration expenditures, and possible equity repurchases in excess of the Company's operating cash flows will depend entirely on the Company's ability to secure acceptable financing, and reasonably priced opportunities. Bank borrowings may be utilized to finance the Company's 2006 capital budget. In addition, the Company will utilize its internal operating cash flows. Future cash flows are subject to a number of variables, including the level of production and oil and natural gas prices. There can be no assurance that operations and other capital resources will provide cash in sufficient amounts to maintain planned levels of capital expenditures or that increased capital expenditures will not be undertaken.

The Company believes that borrowings from financial institutions, projected operating cash flows and the cash on hand will be sufficient to cover its working capital requirements for the next 12 months. In connection with consummating any significant acquisition or funding an exploratory or development drilling program, additional debt or equity financing will be required, which may or may not be available on terms that are acceptable to the Company.

While certain costs are affected by the general level of inflation, factors unique to the oil and natural gas industry result in independent price fluctuations. Over the past five years, significant fluctuations have occurred in oil and natural gas prices. Although it is particularly difficult to estimate future prices of oil and natural gas, price fluctuations have had, and will continue to have, a material effect on the Company. Overall, it is management's belief that inflation is generally favorable to the Company since it does not have significant operating expenses.

## Results of Operations

Three months ended September 30, 2006 compared to Three months ended September 30, 2005.

The Company had net income for the third quarter of 2006 which totaled \$154,153 compared to net income of \$111,763 for the same period in 2005. This increase in income in 2006 was primarily due to the gain on the sale of the leases in Dewitt County, Texas.



Revenues for the third quarter of 2006 totaled \$368,380, a significant increase from revenue in the third quarter of 2005 of \$254,347 primarily because of the gain from the sale of the Edward Dixel Grips lease in Dewitt County. Oil and natural gas sales for the third quarter of 2006 totaled \$231,180, a 6.5% decrease from \$247,288 in the same period in 2005. A decrease in oil prices and natural gas prices were the factors causing this decrease in oil and natural gas sales compared to the same period in 2005. Interest income rose from \$7,059, which was categorized under Other income in the third quarter of 2005 to \$24,657, which is categorized under Interest income in the third quarter of 2006. The Interest income increased because there was an increase in deposits and from the settlement of the Parry v. Amoco Production case. The Interest income attributable to the bank deposits is \$10,804 and the Interest income received from the settlement totaled \$13,853 yielding a combined total of \$24,657.

For the third quarter of 2006, lease operating expenses, which include all production related taxes, totaled \$73,394 compared to \$42,253 incurred for the same period in 2005. In the third quarter of 2006, the Company participated in additional well workovers resulting in higher lease operating costs compared to the same period in 2005 in which the company had less workovers and remedial work. Estimated depreciation and depletion expense for the third quarter of 2006 were unchanged from the third quarter of 2005, at \$12,000.

General and administrative expense, including overhead expense paid to a related party, for the third quarter of 2006, totaled \$55,366 compared to \$47,001 for the same period in 2005. The increase in the general and administrative expense and overhead is due to an increase in legal, accounting and annual report printing fees. Accretion expense for the Asset Retirement accrual was \$7,640 in the third quarter of 2005 compared to \$1,467 in the same period in 2006. The reason for this decrease is the Company established an accretion expense account in the third quarter of 2005, and accrued a higher amount to establish the reserve. The amount reflected in the third quarter of 2006 of \$1,467 is the average quarterly amount of the accretion expense.

Provision for income taxes for the third quarter of 2006 totaled \$72,000 compared to \$29,690 from the same period in 2005. This increase is primarily attributable to an increase in net income for the quarter, which also results in a higher tax bracket.

Nine Months ended September 30, 2006 compared to the Nine months ended September 30, 2005.

Revenues for the nine months ended September 30, 2006, totaled \$ 817,365, a 25% increase from the revenues of \$652,943 at September 30, 2005. The increase is primarily due to the gain on the sale of the Edward Dixel Gips lease in Dewitt County, Texas. Revenue also increased from the settlement of the Parry v. Amoco Production case, in which the Company received disputed past natural gas revenue plus accrued interest. The amount of the settlement was \$20,963 for the natural gas revenue and \$13,852 for the interest that was due, yielding a combined total of \$34,606. The Interest income for the nine months ending September 30, 2006 is attributable to bank deposits is \$10,804, and Interest income received from the settlement totaled \$13,853, yielding a combined total of \$24,657. Other income in the nine months ending September 30, 2005 was \$25,669, which includes sale of equipment, lease bonuses, and Interest income of \$7,060.

Net income for the nine months ended September 30, 2006 totaled \$291,276, and for September 30, 2005, totaled \$197,271. This increase in net income was due to the gain on the sale of the Edward Dixel Gips lease in Dewitt County, Texas, and the settlement amount described in the previous paragraph. Other income in the quarter ending September 30, 2005 included Interest income which was listed separately in 2006. Lease bonuses were listed in Other income in 2005 and in oil & gas income in 2006.

Oil and gas sales for the nine months ended September 30, 2006, totaled \$666,286 a 6% increase from the \$627,274 for the same period in 2005. The increase in oil and gas sales in 2006 compared to 2005 is primarily attributed to a slightly larger number of producing assets in 2006.

Lease operation expense, which includes all production related taxes for the nine months ended September 30, 2006 totaled \$196,552, a 6% decrease from \$209,016 in 2005. Lease operating expenses decreased slightly because of the sale of leases which contributed to expenses in the third quarter of 2006. Depletion and depreciation expense for the nine months ended September 30, 2006 totaled \$36,500 compared to \$33,000 incurred in the nine months ending on September 30, 2005. This increase was due to the small increase in producing assets in 2006. Accretion expense for the Asset Retirement accrual was \$7,640 in the third quarter of 2005 compared to \$4,401 in the same period. This decrease occurred because in 2005 the Company established the asset retirement accruals and expensed the additional amount that needed to be expensed.

General and administrative expenses, including overhead expense paid to related party, for the nine months ended September 30, 2006 totaled \$178,636 compared to \$141,476 for the same period in 2005. The increase in general and administrative and overhead expenses is primarily attributed to the costs of the audit increasing, printing and other costs paid to related third parties, and the higher professional fees of the Company. Part of the increase in legal and accounting costs must be attributed to exploring strategic alternative proposals and in completing the due diligence related to the drafting and review of such proposals. The Company has also incurred additional costs during 2006 associated with compliance with the Sarbanes-Oxley Act of 2002.

Provision for income taxes for the nine months ending September 30, 2006 totaled \$110,000 compared to \$45,540 from the same period in 2005. This increase is due to expected higher income in 2006 which will cause the Company to reach a higher income tax bracket.

#### Recent Accounting Pronouncements

In May 2005, the FASB issued SFAS No. 154, "Accounting Changes and Error Corrections - a replacement of APB Opinion No. 20 and FASB Statement No. 3." SFAS No. 154 replaces APB Opinion ("APB") No. 20, "Accounting Changes", and SFAS No. 3, "Reporting Accounting Changes in Interim Financial Statements," and changed the requirements for the accounting for and reporting of a change in accounting principle. SFAS No. 154 will apply to all voluntary changes in accounting principle as well as to changes required by an accounting pronouncement in the unusual instance that the pronouncement does not include specific transition provisions. APB No. 20 previously required that most voluntary changes in accounting principle be recognized by including in net income of the period of the change the cumulative effect of changing to the new accounting principle. SFAS No. 154 requires retrospective application to prior periods' financial statements of changes in accounting principle, unless it is impracticable to determine either the period-specific effects or the cumulative effect of the change. When it is impracticable to determine the period-specific effects of an accounting change on one or more individual prior periods presented, SFAS No. 154 requires that the new accounting principle be applied to the balances of assets and liabilities as of the beginning of the earliest period for which retrospective application is practicable and that a corresponding adjustment be made to the opening balance of retained earnings (or other appropriate components of equity or net assets in the statement of financial condition).

### **ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

The Company's major market risk exposure is in crude oil and natural gas prices. Realized pricing is primarily driven by the prevailing domestic price for oil and natural gas. Historically, prices received for oil and natural gas production have been volatile and unpredictable. Pricing volatility is expected to continue. Natural gas price realizations for the Nine months ended September 30, 2006, ranged from a monthly low of approximately \$5.00 per Mcf to a monthly high of approximately \$12 per Mcf. Oil prices ranged from a monthly low of approximately \$45 per barrel to a monthly high of approximately \$70 per barrel. A decline in prices of oil or natural gas could have a material adverse effect on the Company's financial condition and results of operations. For the nine months ended September 30, 2006, a 10% reduction in oil and natural gas prices would have reduced revenues by approximately \$66,000

### **ITEM 4. CONTROLS AND PROCEDURES**

#### **Evaluation of Disclosure Controls and Procedures**

The Company maintains controls and procedures designed to ensure that information required to be disclosed by the Company in the reports it files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the Securities and Exchange Commission. At the end of the period covered by this Quarterly Report on Form 10-Q, the Company's management, under the supervision and with the participation of the Company's Chief Executive Officer, evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures. Based on that evaluation, the Company's Chief Executive Officer, after consulting with the audit committee and legal counsel, concluded that as of the end of such period, the Company's disclosure control and procedures are effective in alerting management to material information that is required to be included in the reports the Company files or submits under the Securities Exchange Act of 1934. The Company also maintains an independent Audit Committee of the Board of Directors as part of its internal controls.

#### **Changes in Internal Controls Over Financials Reporting**

There have been no changes in the Company's internal control over financial reporting during the most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

## Part II. Other Information

### ITEM 5. OTHER MATTERS

(a) The resignation of Mr. Edwin W. Peiker, Jr.:

Mr. Edwin W. Peiker, Jr. has elected not to stand for re-election to the Board of Directors. Mr. Harvey Fenster will be nominated to become a replacement director at the Company's annual meeting to be held on December 5, 2006. Certain biographical information about Mr. Fenster will be included in the Company's proxy material, being contemporaneously filed and distributed to shareholders.

### ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits – The following documents are filed as exhibits to this Quarterly Report on Form 10-Q:

31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. \*

31.2 Certification of Acting Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. \*

32.1 Certification of Chief Executive Officer, dated May 12, 2006, pursuant to 18 U.S.C. Section 1350, as adopted to Section 906 of the Sarbanes-Oxley Act of 2002.\*

32.2 Certification of Acting Chief Financial Officer, dated May 12, 2006, pursuant to 18 U.S.C. Section 1350, as adopted to Section 906 of the Sarbanes-Oxley Act of 2002.\*

\* Filed herewith

(b) The following reports on Form 8-K were filed by Registrant during the quarter ended September 30, 2006\*\*:

The Company filed a current report on Form 8-K on July 21, 2006 to announce the sale of significant assets in Dewitt County, Texas to Pool Natural Resources Corporation of Austin, Texas. Pool Natural Resources purchased Croff's lease for the price of \$255,000. These assets included in the sale are as follows:

- The Eyhorn lease which includes a 20% working interest in the Edwards Dixel Gips well and Croff's interest in the Oscar Gips well.
- The Panther Pipeline, approximately 7.2 miles of natural gas pipeline, which Croff recently acquired from Panther Pipeline Ltd. Of Houston, Texas.

\*\* Previously filed



**CERTIFICATIONS**

I, Gerald L. Jensen, certify that :

- As Chief Executive Officer, I have reviewed this quarterly report on Form 10-Q of Croff Enterprises, Inc.;
- Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
- Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
- As Chief Executive Officer, I am responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
  - ◆ Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under my supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to me by others within those entities, particularly during the period in which this report is being prepared;
  - ◆ Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report my conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - ◆ Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
- As Chief Executive Officer, I have disclosed, based on my most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors:
  - ◆ All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - ◆ Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

CROFF ENTERPRISES, INC.

Date: November 1, 2006

By: \_\_\_\_\_ /s/ Gerald L. Jensen

**Gerald L. Jensen,  
President,  
Chief Executive Officer**





## CERTIFICATIONS

I, Gerald L. Jensen, certify that :

- As Acting Chief Financial Officer, I have reviewed this quarterly report on Form 10-Q of Croff Enterprises, Inc.;
- Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
- Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
- As Acting Chief Financial Officer, I am responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
  - ◆ Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under my supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to me by others within those entities, particularly during the period in which this report is being prepared;
  - ◆ Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report my conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - ◆ Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
- As Acting Chief Financial Officer, I have disclosed, based on my most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors:
  - ◆ All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - ◆ Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

CROFF ENTERPRISES, INC.

Date: November 1, 2006

By: /s/ Gerald L. Jensen

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**Gerald L. Jensen,**  
**Acting Chief Financial Officer**



**CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350**

In connection with the Quarterly Report of Croff Enterprises, Inc. (the "Company") on Form 10-Q for the period ended September 30, 2006 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Gerald L. Jensen, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

(1) This Report on form 10Q for the period ended September 30, 2006 fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) I further certify to the best of my knowledge that the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of Croff Enterprises, Inc.

CROFF ENTERPRISES, INC.

Date: November 1, 2006

By: \_\_\_\_\_ /s/ Gerald L. Jensen

**Gerald L. Jensen,  
President,  
Chief Executive Officer**

**CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350**

In connection with the Quarterly Report of Croff Enterprises, Inc. (the "Company") on Form 10-Q for the period ended September 30, 2006 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Gerald L. Jensen, Acting Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

(1) This Report on form 10Q for the period ended September 30, 2006 fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) I further certify to the best of my knowledge that the information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of Croff Enterprises, Inc.

CROFF ENTERPRISES, INC.

Date: November 1, 2006

By: \_\_\_\_\_ /s/ Gerald L. Jensen

**Gerald L. Jensen,**  
**Acting Chief Financial Officer**