

ARENA RESOURCES INC  
Form 10QSB/A  
May 27, 2004

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

**FORM 10-QSB/A**

**Amendment No. 1**

(Mark One)

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

**For the Quarterly Period Ended March 31, 2004**

**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 001-31657

**ARENA RESOURCES, INC.**

(Exact name of registrant as specified in its charter)

Nevada

(State or other jurisdiction of

73-1596109

(I.R.S. Employer

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Incorporation or organization)

Identification No.)

4920 South Lewis Street, Suite 107

Tulsa, Oklahoma 74105

(Address of principal executive officers)

(918) 747-6060

(Issuer's telephone number)

Check whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months, and (2) has been subject to such filing requirements for the past 90 days.  Yes  No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practical date:

As of May 10, 2004, the Company had outstanding 7,192,097 shares of common stock (\$0.001 par value).

Transitional Small Business Disclosure Format (check one): Yes

No

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**Arena Resources, Inc.**

For the Quarter Ended March 31, 2004

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## **Part I Financial Information**

### **Item I. Financial Statements:**

The condensed financial statements included herein have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such rules and regulations, although the Company believes that the disclosures are adequate to make the information presented not misleading.

In the opinion of the Company, all adjustments, consisting of only normal recurring adjustments, necessary to present fairly the financial position of the Company and the results of its operations and its cash flows have been made. The results of its operations and its cash flows for the three months ended March 31, 2004 are not necessarily indicative of the results to be expected for the year ending December 31, 2004.

**CONDENSED BALANCE SHEETS****(UNAUDITED)**

	<b>Pro Forma March 31, 2004 - Note 1</b>	<b>March 31, 2004 (As Restated - Note 1)</b>	<b>December 31, 2003</b>
<b>ASSETS</b>			
<b>Current Assets</b>			
Cash	\$ 1,238,282	\$ 1,238,282	\$ 1,076,676
Account receivable	611,736	424,515	388,910
Short-term investments	25,234	25,234	25,234
Prepaid expenses	32,526	32,526	28,935
<b>Total Current Assets</b>	<b>1,907,778</b>	<b>1,720,557</b>	<b>1,519,755</b>
<b>Property and Equipment, Using Full Cost Accounting</b>			
Oil and gas properties subject to amortization	18,849,527	8,866,225	8,463,400
Drilling advances	244,795	244,795	351,000
Equipment	48,480	48,480	48,480
Office equipment	36,424	36,424	18,978
<b>Total Property and Equipment</b>	<b>19,179,226</b>	<b>9,195,924</b>	<b>8,881,858</b>
Less: Accumulated depreciation and amortization	(611,309)	(611,309)	(513,754)
<b>Net Property and Equipment</b>	<b>18,567,917</b>	<b>8,584,615</b>	<b>8,368,104</b>
<b>Deferred Offering Costs</b>	<b>245,660</b>	<b>245,660</b>	<b>130,872</b>
<b>Total Assets</b>	<b>\$ 20,721,355</b>	<b>\$ 10,550,832</b>	<b>\$ 10,018,731</b>
<b>L I A B I L I T I E S   A N D STOCKHOLDERS' EQUITY</b>			
<b>Current Liabilities</b>			
Accounts payable	\$ 296,002	\$ 194,366	\$ 229,522
Accrued liabilities	71,413	43,413	18,440
Put option	2,905	2,905	2,905

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Short-term note payable	2,000,000	-	-
<b>Total Current Liabilities</b>	<b>2,370,320</b>	<b>240,684</b>	<b>250,867</b>
<b>Long-Term Liabilities</b>			
Notes payable	8,008,440	-	-
Notes payable to related parties	400,000	400,000	400,000
Asset retirement liability	651,943	619,496	607,200
Deferred income taxes	861,273	861,273	671,765
<b>Total Long-Term Liabilities</b>	<b>9,921,656</b>	<b>1,880,769</b>	<b>1,678,965</b>
<b>Stockholders' Equity</b>			
Preferred stock - \$0.001 par value; 10,000,000 shares authorized; no shares issued or outstanding	-	-	-
Common stock - \$0.001 par value; 100,000,000 shares authorized; 7,167,097 shares and 7,162,097 shares outstanding, respectively	7,167	7,167	7,162
Additional paid-in capital	7,019,494	7,019,494	6,994,925
Options and warrants outstanding	810,340	810,340	813,164
Retained earnings	592,378	592,378	273,648
<b>Total Stockholders' Equity</b>	<b>8,429,379</b>	<b>8,429,379</b>	<b>8,088,899</b>
<b>Total Liabilities and Stockholders' Equity</b>	<b>\$ 20,721,355</b>	<b>\$ 10,550,832</b>	<b>\$ 10,018,731</b>

See the accompanying notes to unaudited condensed financial statements.

ARENA RESOURCES, INC.

## CONDENSED STATEMENTS OF OPERATIONS

(UNAUDITED)

<i>For the Three Months Ended March 31,</i>	<b>2004</b>	<b>2003</b>
	<b>(As Restated - Note 1)</b>	
<b>Oil and Gas Revenues</b>	\$ 1,200,400	\$ 807,021
<b>Costs and Operating Expenses</b>		
Oil and gas production costs	316,290	242,071
Oil and gas production taxes	78,707	53,950
Depreciation, depletion and amortization	97,555	51,091
General and administrative expense	178,202	143,631
<b>Total Costs and Operating Expenses</b>	670,754	490,743
<b>Other Income (Expense)</b>		
Gain from change in fair value of put options	-	4,775
Accretion expense	(12,295)	(4,782)
Interest expense	(9,113)	(9,863)
<b>Net Other Expense</b>	(21,408)	(9,870)
<b>Income Before Provision for Income Taxes and Cumulative Effect of Change in Accounting Principle</b>	508,238	306,408
<b>Provision for Deferred Income Taxes</b>	189,508	114,289
<b>Income Before Cumulative Effect of Change in Accounting Principle</b>	318,730	192,119
<b>Cumulative Effect of Change in Accounting Principle</b>	-	(11,813)
<b>Net Income</b>	\$ 318,730	\$ 180,306



**Basic Income Per Common Share**

Before cumulative effect of change in accounting principle	\$	0.04	\$	0.03
Net Income		0.04		0.03

**Diluted Income Per Common Share**

Before cumulative effect of change in accounting principle	\$	0.04	\$	0.03
Net Income		0.04		0.03

See the accompanying notes to unaudited condensed financial statements.

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ARENA RESOURCES, INC.

CONDENSED STATEMENTS OF CASH FLOWS

(UNAUDITED)

*For the Three Months Ended March 31,*

	<b>2004</b>	<b>2003</b>
	<b>(As Restated</b>	
	<b>- Note 1)</b>	
<b>Cash Flows From Operating Activities</b>		
Net income	\$ 318,730	\$ 180,306
Adjustments to reconcile net income to net cash provided by operating activities:		

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Depreciation, depletion and amortization	97,555	51,091
Gain from change in fair value of put option	-	(4,776)
Cumulative effect of change in accounting principle	-	11,813
Accretion of discounted liabilities	12,295	4,782
Changes in assets and liabilities:		
Accounts receivable	(35,605)	(5,454)
Prepaid expenses	(3,591)	(1,000)
Accounts payable and accrued liabilities	(10,182)	(72,784)
Deferred income taxes	189,508	114,287
<b>Net Cash Provided by Operating Activities</b>	<b>568,710</b>	<b>278,265</b>
<b>Cash Flows from Investing Activities</b>		
Purchase of oil and gas properties	(296,620)	(153,715)
Purchase of office equipment	(17,446)	-
<b>Net Cash Used in Investing Activities</b>	<b>(314,066)</b>	<b>(153,715)</b>
<b>Cash Flows From Financing Activities</b>		
Proceeds from issuance of common stock and warrants less offering costs paid	(114,788)	183,739
Proceeds from exercise of warrants	21,750	-
Collection of common stock subscription receivable	-	157,500
Payment of accrued dividends to preferred stockholders	-	(46,384)
<b>Net Cash Provided by (Used in) Financing Activities</b>	<b>(93,038)</b>	<b>294,855</b>
<b>Net Increase in Cash</b>	<b>161,606</b>	<b>419,405</b>
<b>Cash at Beginning of Period</b>	<b>1,076,676</b>	<b>796,915</b>
<b>Cash at End of Period</b>	<b>\$ 1,238,282</b>	<b>\$ 1,216,320</b>
<b>Supplemental Cash Flows Information</b>		
Cash paid for interest	\$ 9,863	\$ 9,866

See the accompanying notes to unaudited condensed financial statements.

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**ARENA RESOURCES, INC.**

**NOTES TO UNAUDITED CONDENSED FINANCIAL STATEMENTS**

**MARCH 31, 2004**

**NOTE 1 BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES**

*Condensed Financial Statements* The accompanying condensed financial statements have been prepared by the Company and are unaudited. In the opinion of management, the accompanying unaudited financial statements contain all adjustments necessary for fair presentation, consisting of normal recurring adjustments, except as disclosed herein.

The accompanying unaudited interim financial statements have been condensed pursuant to the rules and regulations of the Securities and Exchange Commission; therefore, certain information and disclosures generally included in financial statements have been condensed or omitted. The condensed financial statements should be read in conjunction with the Company's annual financial statements included in its annual report on Form 10-KSB as of December 31, 2003. The financial position and results of operations for the three months ended March 31, 2004 are not necessarily indicative of the results to be expected for the full year ending December 31, 2004.

*Nature of Operations* The Company owns interests in oil and gas properties located in Oklahoma, Texas, Kansas and New Mexico. The Company is engaged primarily in the acquisition, exploration and development of oil and gas properties and the production and sale of oil and gas.

*Use of Estimates* The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

**Pro Forma Balance Sheet** On May 7, 2004, the Company acquired a working interest in the East Hobbs San Andres Property mineral lease as described more fully in Note 3. In order to facilitate the closing of the acquisition, on May 7, 2004, the Company borrowed \$8,008,440 under the terms of a long-term revolving credit facility and borrowed \$2,000,000 under the terms of a short-term bridge financing arrangement; the terms of which are both described in Note 4. The accompanying pro forma condensed balance sheet as of March 31, 2004 has been prepared to present the estimated effects of the acquisition and these financing transactions on the financial position of the Company as if they had occurred on March 31, 2004.

**Oil and Gas Properties** The Company uses the full cost method of accounting for oil and gas properties. Under this method, all costs associated with acquisition, exploration, and development of oil and gas reserves are capitalized. Costs capitalized include acquisition costs, geological and geophysical expenditures, lease rentals on undeveloped properties and costs of drilling and equipping productive and non-productive wells. Drilling costs include directly related overhead costs. Capitalized costs are categorized either as being subject to amortization or not subject to amortization.

All capitalized costs of oil and gas properties, including the estimated future costs to develop proved reserves and estimated future costs of abandonment and site restoration, are amortized on the unit-of-production method using estimates of proved reserves as determined by independent engineers. Investments in unproved properties and major development projects are not amortized until proved reserves associated with the projects can be determined. The Company evaluates oil and gas properties for impairment at least quarterly. If the results of an assessment indicate that the properties are impaired, the amount of the impairment is added to the capitalized costs to be amortized. Amortization expense for the three months ended March 31, 2004 was \$97,555 based on depletion at the rate of \$2.64 per barrel of oil equivalent compared to \$51,091 based on depletion at the rate of \$1.88 per barrel of oil equivalent for the

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three months ended March 31, 2003. These amounts include \$3,299 and \$2,376 of depreciation on equipment during the three months ended March 31, 2004 and 2003, respectively.

In addition, capitalized costs are subject to a ceiling test which limits such costs to the estimated present value of future net revenues from proved reserves, discounted at a 10-percent interest rate, based on current economic and operating conditions, plus the lower of cost or fair market value of unproved properties. Consideration received from sales or transfers of oil and gas property is accounted for as a reduction of capitalized costs. Revenue is not recognized in connection with contractual services performed in connection with properties in which the Company holds an ownership interest.

**Income Per Common Share** Basic income per common share is computed by dividing net income by the weighted-average number of common shares outstanding during the period. Diluted income per share reflects the potential dilution that could occur if all contracts to issue common stock were converted into common stock, except for those that are anti-dilutive.

**Concentration of Credit Risk and Major Customer** The Company currently has cash in excess of federally insured limits at March 31, 2004. During the three months ended March 31, 2004, sales to three customers represented 47%, 24% and 17% of total sales, respectively. At March 31, 2004, these three customers made up 39%, 29% and 15% of accounts receivable, respectively.

**Stock-Based Employee Compensation** The Company applies the recognition and measurement principles of Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees* (APB 25) and related interpretations in accounting for its stock-based compensation awards to employees. Under APB 25, no stock-based compensation expense was charged to earnings, as all options granted had an exercise price equal to or greater than the adjusted fair value of the underlying common stock on the grant date.

Alternately, Statement on Financial Accounting Standards No. 123, *Accounting for Stock-Based Compensation* (SFAS No. 123), allows companies to recognize compensation expense over the related service period based on the grant date fair value of the stock option awards. The following table illustrates the effect on net income and basic and diluted income per common share if the Company had applied the fair value recognition provisions of SFAS No. 123 to stock-based employee compensation:

<b>For the Three Months Ended March 31,</b>	<b>2004</b>	<b>2003</b>
Net income, as reported	\$ 318,730	\$ 180,306
Deduct: Total stock-based employee compensation expense determined under the fair value based method for all awards, net of related tax effects	(127,099)	-
Pro Forma Net Income	\$ 191,631	\$ 180,306
Income per Common Share		
Basic, as reported	\$ 0.04	\$ 0.03
Basic, pro forma	0.03	0.03
Diluted, as reported	0.04	0.03
Diluted, pro forma	0.02	0.03

**Restatement** The Company has restated the accompanying condensed financial statements as of March 31, 2004 and for the three months then ended to reflect the effects of correcting the date of the acquisition of the East Hobbs San Andres Property mineral lease from March 1, 2004 to May 7, 2004. The effects of the restatement are as follows:

	<b>As Previously Reported</b>	<b>Effect of Restatement</b>	<b>As Restated</b>
<b>As of March 31, 2004</b>			
Current assets	\$ 1,947,678	\$ (227,121)	\$ 1,720,557
Property and equipment, net	18,688,054	(10,103,439)	8,584,615
Total assets	20,881,392	(10,330,560)	10,550,832
Current liabilities	10,464,429	(10,223,745)	240,684
Long-term liabilities	1,937,916	(57,147)	1,880,769
Stockholders' equity	8,479,047	(49,668)	8,429,379
<b>For the Three Months Ended March 31, 2004</b>			
Revenue	\$ 1,409,719	\$ (209,319)	\$ 1,200,400
Costs and operating expenses	805,704	(134,950)	670,754
Income before provision for income taxes	582,369	(74,131)	508,238
Provision for income taxes	213,971	(24,463)	189,508
Net income	368,398	(49,668)	318,730
Basic income per common share	0.05	(0.01)	0.04
Diluted income per common share	0.05	(0.01)	0.04

## NOTE 2 EARNINGS PER SHARE INFORMATION

<b>For the Three Months Ended March 31,</b>	<b>2004</b>	<b>2003</b>
Income before cumulative effect of change in accounting principle	318,730	192,119
Cumulative effect of change in accounting principle	-	(11,813)
Net Income	\$ 318,730	\$ 180,306
Basic weighted-average common shares outstanding	7,163,734	6,327,609
Effect of dilutive securities		
Warrants	429,739	133,482
Stock options	243,441	-
Diluted Weighted-Average Common Shares Outstanding	7,836,914	6,461,091
Basic Income Per Common Share		

Before cumulative effect of change in accounting principle	\$	0.04	\$	0.03
Cumulative effect of change in accounting principle		-		-
Net Income Attributable to Common Shares	\$	0.04	\$	0.03
Diluted Income Per Common Share				
Before cumulative effect of change in accounting principle	\$	0.04	\$	0.03
Cumulative effect of change in accounting principle		-		-
Net Income Attributable to Common Shares	\$	0.04	\$	0.03

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### NOTE 3 ACQUISITION OF OIL AND GAS PROPERTIES

On May 7, 2004, the Company acquired an 82.24% working interest, 67.60% net revenue interest, in the East Hobbs San Andres Property mineral lease ( East Hobbs ) located in Lea County, New Mexico. Although the Purchase and Sales Agreement transferred the revenue and the related operating costs from East Hobbs to Arena beginning March 1, 2004, Arena did not control the property interests until May 7, 2004. As a result, the acquisition date for accounting purposes was May 7, 2004 and the operations of East Hobbs operations will be included in the results of operations of Arena from May 7, 2004. Revenues and operating costs for the months of March and April have been estimated and treated as adjustments to the purchase price. Those estimates are subject to adjustment when actual information is available; thus, the purchase price and the allocation of the purchase price are subject to refinement.

East Hobbs is comprised of 20 operating oil and gas wells that were unitized into one lease prior to the acquisition. The Company purchased East Hobbs for its current production and cash flow, as well as for the drilling and secondary recovery opportunities from the property. The purchase price was \$10,036,440 and consisted of \$10,008,440 of cash and \$28,000 of estimated acquisition costs. The acquisition was funded through the use of a credit facility and bridge financing described more fully in Note 4. The purchase price was allocated to the assets acquired and the liabilities assumed as follows:

Accounts receivable	\$	187,221
Oil and gas properties subject to amortization		9,983,302
Total Assets Acquired		10,170,523
Accounts payable		(101,636)
Asset retirement obligation		(32,447)
Total Liabilities Assumed		(134,083)

Net Assets Acquired \$ 10,036,440

The following pro forma information is presented to reflect the operations of the Company as if the acquisition of East Hobbs had been completed on January 1, 2004 and 2003, respectively:

<i>For the Three Months Ended March 31,</i>	<b>2004</b>	<b>2003</b>
<b>Oil and Gas Revenues</b>	\$ 1,813,406	\$ 1,481,834
<b>Income from Operations Before Cumulative Effect of Change in Accounting Principle</b>	494,832	399,627
<b>Net Income</b>	494,832	387,814
<b>Basic Income Per Common Share</b>		
Income before cumulative effect of change in accounting principle	\$ 0.07	\$ 0.06
Net income	0.07	0.06
<b>Diluted Income Per Common Share</b>		
Income before cumulative effect of change in accounting principle	\$ 0.06	\$ 0.06
Net income	0.06	0.06

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#### **NOTE 4 NOTES PAYABLE**

On February 3, 2003, the Company established a \$10,000,000 revolving credit facility with a bank with an initial borrowing base of \$2,000,000. On December 31, 2003, the Company entered into an agreement that increased the revolving credit facility to \$20,000,000 and increased the initial borrowing base to \$4,000,000. On April 14, 2004, the Company changed financial institutions and thereby canceled this credit facility.

On April 14, 2004, the Company established a new \$15,000,000 credit facility from a bank with an \$8,500,000 initial borrowing base. Any increases in the borrowing base are subject to written consent by the financial institution. The interest rate is a floating rate equal to the 30, 60 or 90 day LIBOR plus 2.25%, currently 3.42% per annum, and is payable monthly. Annual fees for the facility are 1/8 of one percent of the unused portion of the borrowing base.



Amounts borrowed under the revolving credit facility are due in April 2007. The revolving credit facility is secured by the Company's principal mineral interests. In order to obtain the revolving credit facility, loans from two officers were subordinated to the position of the bank. The Company is required under the terms of the credit facility to maintain a tangible net worth of \$6,000,000, maintain a 5-to-1 ratio of income before interest, taxes, depreciation, depletion and amortization to interest expense and maintain a current asset to current liability ratio of 1-to-1, not including the \$2,000,000 bridge financing arrangement discussed below. On May 7, 2004, the Company drew \$8,008,440 under this revolving credit facility to fund the acquisition of the East Hobbs San Andres Property interests. An additional \$294,029 is reserved under the revolving credit facility as collateral for standby letters of credit issued to various states.

On April 14, 2004, the Company also entered into a bridge financing arrangement for \$2,000,000 from a bank. On May 7, 2004, the Company borrowed \$2,000,000 under the terms of the bridge financing arrangement to fund the acquisition of the East Hobbs San Andres Property interests. The interest rate on the bridge financing arrangement is a floating rate equal to the 30, 60 or 90 day LIBOR plus 2.25%, currently 3.42% per annum, and is payable monthly. The bridge financing arrangement has been guaranteed by two of the Company's officers. Amounts borrowed under the bridge financing arrangement are due June 30, 2004.

On April 13, 2004, the Board of Directors agreed to an extension of the notes payable to two of its officers to July 1, 2005, under the same terms as the original notes.

**NOTE 5 ASSET RETIREMENT OBLIGATION**

The asset retirement obligation is adjusted each quarter for any liabilities incurred or settled during the period, accretion expense and any revisions made to the estimated cash flows. The reconciliation of the asset retirement obligation for the three months ended March 31, 2004 is as follows:

Balance, January 1, 2004	\$ 607,200
Accretion expense	12,295
Balance, March 31, 2004	\$ 619,495

**NOTE 6 - STOCKHOLDERS EQUITY**

*Warrants exercised* During the three months ended March 31, 2004, the Company issued 5,000 shares of common stock from the exercise of warrants. Of the 5,000 warrants, 1,000 had an exercise price of \$1.75 per share and 4,000 had an exercise price of \$5.00 per share; therefore, the Company received \$21,750 from the exercise.

**NOTE 7 CONTINGENCIES AND COMMITMENTS**

*Standby Letters of Credit* A commercial bank has issued standby letters of credit on behalf of the Company to the states of Texas, Oklahoma and New Mexico totaling \$294,029 to allow the Company to do business in those states.

The standby letters of credit are valid through May 2005 and are collateralized by the revolving credit facility with the bank. The Company intends to renew the standby letters of credit for as long as the Company does business in those states. No amounts have been drawn under the standby letters of credit.

**NOTE 8 - SUBSEQUENT EVENTS**

Subsequent to March 31, 2004, the Company has received \$108,750 from exercise of 5,000 warrants that had an exercise price of \$1.75 per share and the exercise of 20,000 warrants that had an exercise price of \$5.00 per share.

On April 14, 2004, the Company changed financial institutions and established a new revolving credit facility and a bridge financing agreement as of that same date, as further disclosed in Note 4.

On May 7, 2004, the Company closed the acquisition of the East Hobbs San Andres Property interest as further discussed in Note 3.

## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

### *Results of Operations*

*Oil and natural gas sales.* For the three months ended March 31, 2004, oil and natural gas sales revenue increased \$393,379 to \$1,200,400, compared to \$807,021 for the same period during 2003. Oil sales increased \$363,996 and natural gas sales increased \$29,383. The increase in oil sales was the result of a sales volume increase of 10,193 barrels for the three months ended March 31, 2004 compared to the same period in 2003, and a 3% increase in the average realized per barrel oil price from \$32.38 for the three months ended March 31, 2003 to \$33.23 for the three months ended March 31, 2004. The increase in natural gas sales was the result of a sales volume increase of 8,411 thousand cubic feet (MCF) for the three months ended March 31, 2004 compared to the same period in 2003, offset by a 9% decrease in the average realized natural gas price per MCF from \$4.40 for the three months ended March 31, 2003 to \$4.00 for the three months ended March 31, 2004. The volume increase for crude oil and natural gas primarily resulted from \$3 million of capital expenditures during 2003.

*Lease operating expenses.* Our lease operating expenses increased from \$242,071 or \$9.52 per barrel of oil equivalent (BOE) for the three months ended March 31, 2004 to \$316,290 or \$8.54 per BOE for the three months ended March 31, 2004. This increase was a result of higher operating costs on properties acquired in 2003. While it is possible that this increase will continue in the future as we acquire additional properties, because each property is individual in its characteristics, at this time, apart from normal increases associated with inflation in general, we cannot specifically identify this increase to be a trend.

*Production taxes.* Production taxes as a percentage of oil and natural gas sales were 7% during the three months ended March 31, 2003 and remained steady at 7% for the three months ended March 31, 2004. Production taxes vary from state to state. Therefore, these taxes are likely to vary in the future depending on the mix of production we generate from various states, as well as the possibility that any state may raise its production tax.

*Depreciation, depletion and amortization.* Our depreciation, depletion and amortization expense increased by \$46,464 to \$97,555 for the three months ended March 31, 2004, compared to the same period in 2003. The increase was a result of an increase in the average depreciation, depletion and amortization rate from \$1.88 per BOE during the three months ended March 31, 2003 to \$2.64 per BOE during the three months ended March 31, 2004. The increased depreciation, depletion and amortization was the result of increased sales volume and an increase in estimated future development costs, which increases the per BOE depreciation, depletion and amortization rate.

*General and administrative expenses.* General and administrative expenses increased by \$34,571 to \$178,202 for the three months ended March 31, 2004. This increase was primarily related to increases in compensation expense associated with an increase in personnel required to administer our growth and \$16,095 paid to Lee Keeling &

Associates for the preparation of reserve analysis reports for the year ended December 31, 2003.

*Interest expense (net of interest income).* Interest expense decreased \$749 to \$9,114 for the three months ended March 31, 2004 when compared to the same period in 2003. The decrease was due to earning interest on part of our available cash balance in order to offset a portion of the interest expense incurred.

*Income tax expense.* Our effective tax rate was 37% during the three months ended March 31, 2003 and remained steady at 37% for the three months ended March 31, 2004.

*Net income.* Net income increased from \$180,306 for the three months ended March 31, 2003 to \$318,730 for 2004. The primary reasons for this increase include higher crude oil prices between periods

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and an increase in volumes sold, partially offset by higher lease operating expense, income tax expense and general and administrative expenses due to our growth.

*Revenues Year to Date by Geographic section*

Arena reports its net oil and gas revenues for the year to date as applicable to the following geographic sectors:

**OIL**

Net Production Volume

Net Revenue

Texas Leases

9,051 BBLs

\$ 300,348

Oklahoma Leases

15,827 BBLs

\$ 539,576

New Mexico Leases

8,905 BBLs

\$ 282,788

**GAS**

Net Production Volume

Net Revenue

Texas Leases 3,501 MCF

\$ 10,123

Oklahoma Leases 8,706 MCF

\$ 29,766

New Mexico Leases 7,116 MCF

\$ 37,477

*Significant Subsequent Events Occurring after March 31, 2004:*

Subsequent to March 31, 2004, the Company has received \$108,750 from exercise of 5,000 warrants that had an exercise price of \$1.75 per share and the exercise of 20,000 warrants that had an exercise price of \$5.00 per share.

On April 14, 2004, the Company changed financial institutions and established a new revolving credit facility and a bridge financing agreement as of that same date, as further disclosed in Note 4.

On May 7, 2004, the Company closed the acquisition of the East Hobbs San Andres Unit as further discussed in note 3.

The following pro forma information is presented to reflect the operations of the Company as if the acquisition of East Hobbs had been completed on January 1, 2004 and 2003, respectively:

<i>For the Three Months Ended March 31,</i>	<b>2004</b>	<b>2003</b>
<b>Oil and Gas Revenues</b>	\$ 1,813,406	\$ 1,481,834
<b>Income from Operations Before Cumulative Effect of Change in Accounting Principle</b>	494,832	399,627
<b>Net Income</b>	494,832	387,814
<b>Basic Income Per Common Share</b>		
Income before cumulative effect of change in accounting principle	\$ 0.07	\$ 0.06
Net income	0.07	0.06
<b>Diluted Income Per Common Share</b>		
Income before cumulative effect of change in accounting principle	\$ 0.06	\$ 0.06
Net income	0.06	0.06

As shown in the financial statements for the three months ended March 31, 2004, the Company had cash on hand of \$1,238,282, compared to \$1,076,676 as of December 31, 2003. The Company had positive net cash flows from operations for the three months ended March 31, 2004 of \$568,710, compared to \$278,265 for the same period 2003. Other significant sources of cash inflow in 2003 were the common stock private placement with net proceeds in 2003 of \$183,739 and the collection of a common stock subscription receivable, in the amount of \$157,500. The most significant cash outflows during the three months ended March 31, 2004 and 2003 were capital expenditures of \$296,620 in 2004 and 153,715 in 2003 and payment of preferred stock dividends of \$46,384 in 2003.

On February 3, 2003, the Company established a \$10,000,000 revolving credit facility with a bank with an initial borrowing base of \$2,000,000. On December 31, 2003, the Company entered into an agreement that increased the revolving credit facility to \$20,000,000 and increased the initial borrowing base to \$4,000,000. On April 14, 2004, the Company changed financial institutions and thereby canceled this credit facility.

On April 14, 2004, the Company established a new \$15,000,000 credit facility from a bank with an \$8,500,000 initial borrowing base. Any increases in the borrowing base are subject to written consent by the financial institution. The interest rate is a floating rate equal to the 30, 60 or 90 day LIBOR plus 2.25%, currently 3.42% per annum, and is payable monthly. Annual fees for the facility are 1/8 of one percent of the unused portion of the borrowing base. Amounts borrowed under the revolving credit facility are due in April 2007. The revolving credit facility is secured by the Company's principal mineral interests. In order to obtain the revolving credit facility, loans from two officers were subordinated to the position of the bank. The Company is required under the terms of the credit facility to maintain a tangible net worth of \$6,000,000, maintain a 5-to-1 ratio of income before interest, taxes, depreciation, depletion and amortization to interest expense and maintain a current asset to current liability ratio of 1-to-1, not including the \$2,000,000 bridge financing arrangement discussed below. On May 7, 2004, the Company drew \$8,008,440 under this revolving credit facility to fund the acquisition of the East Hobbs San Andres Property interests. An additional \$294,029 is reserved under the revolving credit facility as collateral for standby letters of credit issued to various states.

On April 14, 2004, the Company also entered into a bridge financing arrangement for \$2,000,000 from a bank. On May 7, 2004, the Company borrowed \$2,000,000 under the terms of the bridge financing arrangement to fund the acquisition of the East Hobbs San Andres Property interests. The interest rate on the bridge financing arrangement is a floating rate equal to the 30, 60 or 90 day LIBOR plus 2.25%, currently 3.42% per annum, and is payable monthly. The bridge financing arrangement has been guaranteed by two of the Company's officers. Amounts borrowed under the bridge financing arrangement are due June 30, 2004.

Management plans to continue to make acquisitions, using net cash flows from operations and possibly the above referenced credit facility and additional equity capital.

*Disclosures About Market Risks*

Like other natural resource producers, Arena faces certain unique market risks. The two most salient risk factors are the volatile prices of oil and gas and certain environmental concerns and obligations.

### Oil and Gas Prices

Current competitive factors in the domestic oil and gas industry are unique. The actual price range of crude oil is largely established by major international producers. Pricing for natural gas is more regional. Because domestic demand for oil and gas exceeds supply, there is little risk that all current production

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will not be sold at relatively fixed prices. To this extent Arena does not see itself as directly competitive with other producers, nor is there any significant risk that the company could not sell all production at current prices with a reasonable profit margin. The risk of domestic overproduction at current prices is not deemed significant. The primary competitive risks would come from falling international prices which could render current production uneconomical.

Secondarily, Arena is presently committed to use the services of the existing gatherers in its present areas of production. This gives to such gatherers certain short term relative monopolistic powers to set gathering and transportation costs, because obtaining the services of an alternative gathering company would require substantial additional costs since an alternative gatherer would be required to lay new pipeline and/or obtain new rights of way in the lease.

It is also significant that more favorable prices can usually be negotiated for larger quantities of oil and/or gas product, such that Arena views itself as having a price disadvantage to larger producers. Large producers also have a competitive advantage to the extent they can devote substantially more resources to acquiring prime leases and resources to better find and develop prospects.

### Environmental

Oil and gas production is a highly regulated activity which is subject to significant environmental and conservation regulations both on a federal and state level. Historically, most of the environmental regulation of oil and gas production has been left to state regulatory boards or agencies in those jurisdictions where there is significant gas and oil production, with limited direct regulation by such federal agencies as the Environmental Protection Agency.



However, while the Company believes this generally to be the case for its production activities in Texas, Oklahoma, Kansas and New Mexico, it should be noticed that there are various Environmental Protection Agency regulations which would govern significant spills, blow-outs, or uncontrolled emissions.

In Oklahoma, Texas, Kansas and New Mexico specific oil and gas regulations exist related to the drilling, completion and operations of wells, as well as disposal of waste oil. There are also procedures incident to the plugging and abandonment of dry holes or other non-operational wells, all as governed by the Oklahoma Corporation Commission, Oil and Gas Division, the Texas Railroad Commission, Oil and Gas Division, the Kansas Corporation Commission, Oil and Gas Division or the New Mexico Oil Conservation Division.

Compliance with these regulations may constitute a significant cost and effort for Arena. No specific accounting for environmental compliance has been maintained or projected by Arena to date. Arena does not presently know of any environmental demands, claims, or adverse actions, litigation or administrative proceedings in which it or the acquired properties are involved or subject to or arising out of its predecessor operations.

In the event of a breach of environmental regulations, these environmental regulatory agencies have a broad range of alternative or cumulative remedies to include: ordering a clean up of any spills or waste material and restoration of the soil or water to conditions existing prior to the environmental violation; fines; or enjoining further drilling, completion or production activities. In certain egregious situations the agencies may also pursue criminal remedies against the Company or its principals.

#### *Forward-Looking Information*

Certain statements in this Section and elsewhere in this report are forward-looking in nature and relate to trends and events that may affect the Company's future financial position and operating results. Such statements are made pursuant to the safe harbor provision of the *Private Securities Litigation Reform Act of 1995*. The terms "expect," "anticipate," "intend," and "project" and similar words or expressions are intended to identify forward-looking statements. These statements speak only as of the date of this report.

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The statements are based on current expectations, are inherently uncertain, are subject to risks, and should be viewed with caution. Actual results and experience may differ materially from the forward-looking statements as a result of many factors, including changes in economic conditions in the markets served by the company, increasing competition, fluctuations in raw materials and energy prices, and other unanticipated events and conditions. It is not possible to foresee or identify all such factors. The company makes no commitment to update any forward-looking

statement or to disclose any facts, events, or circumstances after the date hereof that may affect the accuracy of any forward-looking statement.

### **Item 3. Controls and Procedures**

(a)

The Company maintains controls and procedures designed to ensure that information required to be disclosed in the reports that the Company 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. Specifically, the Company maintains an independent audit committee to monitor internal controls and procedures. Based upon their evaluation of those controls and procedures performed within 90 days of the filing date of this report, the chief executive officer and the principal financial officer of the Company concluded that the Company's disclosure controls and procedures were adequate. The Company is not aware of any fraud or any material irregularities from its accounting or auditing procedures.

(b)

Changes in internal controls. The Company made no significant changes in its internal controls or in other factors that could significantly affect these controls subsequent to the date of the evaluation of those controls by the chief executive officer and principal financial officer.

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## **Part II - Other Information**

### **Item 1. Legal Proceedings**

None.

**Item 2. Changes in Securities and Small Business Issuers Purchases of Equity Securities**

None.

**Item 3. Defaults Upon Senior Securities**

None.

**Item 4. Submission of Matters to a Vote of Security Holders**

None.

**Item 5. Other Information**

None.

**Item 6. Exhibits and Reports on Form 8-K**

(a)

Exhibit 31.1

Section 302 Certification of CEO

Exhibit 31.2

Section 302 Certification of CFO

(b)

Exhibit 32.1

Section 1350 Certification of CEO

Exhibit 32.2

Section 1350 Certification of CFO

(c)

There were no 8-K filings during the quarter ending March 31, 2004.

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**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

REGISTRANT: **ARENA RESOURCES, INC.**

Dated: May 27, 2004

By: /s/ Lloyd Tim Rochford

Lloyd Tim Rochford

President, Chief Executive Officer

Dated: May 27, 2004

By: /s Stanley McCabe

Stanley McCabe

Treasurer, Secretary

Dated: May 27, 2004

By: /s/ William R. Broaddrick

William R. Broaddrick

Vice President, Chief Financial Officer

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**Exhibit 31.1**

**SECTION 302 CERTIFICATION**

CERTIFICATION

I, Lloyd T. Rochford, certify that:

Edgar Filing: ARENA RESOURCES INC - Form 10QSB/A

1. I have reviewed this quarterly report on Form 10-QSB/A of Arena Resources, Inc.;
  
2. Based on my knowledge, this quarterly 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 quarterly report;
  
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly 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 quarterly report;
  
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and have:
  - a) designed such disclosure controls and producers to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
  
  - b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and
  
  - c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
  
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):
  - a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
  
  - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

May 27, 2004

Date

/s/ Lloyd T. Rochford

Lloyd T. Rochford

Chief Executive Officer

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**Exhibit 31.2**

**SECTION 302 CERTIFICATION**

CERTIFICATION

I, William R. Broaddrick, certify that:

1. I have reviewed this quarterly report on Form 10-QSB/A of Arena Resources, Inc.;

2. Based on my knowledge, this quarterly 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 quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly 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 quarterly report;

4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and have:

a) designed such disclosure controls and producers to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;

b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and

c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):

a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to



the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

May 27, 2004

Date

/s/ William R. Broaddrick

William R. Broaddrick

Chief Financial Officer

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**Exhibit 32.1**

**SECTION 906 CERTIFICATIONS**

**CERTIFICATION PURSUANT TO**

**18 U.S.C. SECTION 1350,**

**AS ADOPTED PURSUANT TO**

**SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Arena Resources, Inc. (the Company) on Form 10-QSB/A for the period ending March 31, 2004, as filed with the Securities and Exchange Commission on the date hereof (the Report), I, Lloyd T. Rochford, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted

pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to the best of my knowledge and belief:

(1)

the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2)

the information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

/s/ Lloyd T. Rochford

Lloyd T. Rochford

Chief Executive Officer

May 27, 2004

A signed original of this written statement required by Section 906, or other document authenticating, acknowledging, or otherwise adopting the signature that appears in typed form within the electronic version of this written statement has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

**Exhibit 32.2**

**SECTION 906 CERTIFICATIONS**

**CERTIFICATION PURSUANT TO**

**18 U.S.C. SECTION 1350,**

**AS ADOPTED PURSUANT TO**

**SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Arena Resources, Inc. (the Company) on Form 10-QSB/A for the period ending March 31, 2004, as filed with the Securities and Exchange Commission on the date hereof (the Report), I, William R. Broaddrick, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to the best of my knowledge and belief:

(1)

the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2)

the information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

/s/ William R. Broaddrick

William R. Broaddrick

Chief Financial Officer

May 27, 2004

A signed original of this written statement required by Section 906, or other document authenticating, acknowledging, or otherwise adopting the signature that appears in typed form within the electronic version of this written statement has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.