

TETON ENERGY CORP
Form 10-Q
November 14, 2005

U.S. SECURITIES AND EXCHANGE COMMISSION

Washington, D. C. 20549

FORM 10-Q

(Mark One)

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

For the Quarterly Period Ended September 30, 2005

TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT
OF 1934

For the transition period from _____ to _____

Commission file number: 001-31679

TETON ENERGY CORPORATION

(Exact Name of Registrant as Specified in its Charter)

Delaware
(State or Other Jurisdiction of
Incorporation or Organization)

84-1482290
(I.R.S. Employer
Identification No.)

(303) - 565-4600

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(Registrant's Telephone Number including area code)

410 17th Street, Suite 1850

Denver, Colorado 80202-4444

(Address of Principal Executive Office)

Indicate by check mark whether the registrant (1) filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act 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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

As of November 7, 2005, 11,303,745 shares of the issuer's common stock were outstanding.

TETON ENERGY CORPORATION

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PART I. FINANCIAL INFORMATION

TETON ENERGY CORPORATION

Consolidated Balance Sheets

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	September 30, 2005 (Unaudited)	December 31, 2004
Assets		
Current assets		
Cash and cash equivalents	\$ 7,969,202	\$ 17,433,424
Trade accounts receivable	127,470	
Advances to operator	226,651	
Prepaid expenses and other assets	184,642	100,917
Total current assets	8,507,965	17,534,341
Non-current assets		
Oil & Gas properties (using successful efforts method of accounting)		
Proved	981,435	
Unproved	10,564,322	
Wells in progress	210,277	
Facilities in progress	30,681	
Fixed assets	69,993	64,621
Total property and equipment	11,856,708	64,621
Less accumulated depreciation and depletion	(96,628)	(12,397)
Net property and equipment	11,760,080	52,224
Other assets		25,000
Total non-current assets	11,760,080	77,224
Total assets	\$ 20,268,045	\$ 17,611,565
Liabilities and Stockholders' Equity		
Current liabilities		
Accounts payable and accrued liabilities	\$ 572,639	\$ 411,745
Royalties and payroll taxes payable	117,385	
Total current liabilities	690,024	411,745
Long-term liability		
Asset retirement obligation	2,543	
Commitments and contingencies		
Stockholders' equity		
Series A convertible preferred stock, \$.001 par value, 25,000,000 shares authorized, 0 and 281,460 issued and outstanding at September 30, 2005 and December 31, 2004. Liquidation preference at September 30, 2005 and December 31, 2004 of \$0 and \$1,248,838, respectively		281
Common stock, \$.001 par value, 250,000,000 shares authorized, 11,162,245 and 9,130,257 shares issued and outstanding at September 30, 2005 and December 31, 2004, respectively	11,162	9,130
Additional paid-in capital	43,134,078	37,657,686
Accumulated deficit	(23,569,762)	(20,467,277)
Total stockholders' equity	19,575,478	17,199,820
Total liabilities and stockholders' equity	\$ 20,268,045	\$ 17,611,565

See notes to unaudited consolidated financial statements.

TETON ENERGY CORPORATION

Unaudited Consolidated Statements of Operations and Comprehensive Income (Loss)

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	For the Three Months Ended September 30,	
	2005	2004
Oil and gas sales	\$ 229,594	\$
Cost of sales and expenses:		
Lease operating expenses	3,000	
Production taxes	16,086	
General and administrative	771,951	521,140
Depletion, depreciation and amortization	74,381	3,481
Exploration	216,209	
Total cost of sales and expenses	1,081,627	524,621
Loss from operations	(852,033)	(524,621)
Other income		
Other income	49,748	36,495
Total other income	49,748	36,495
Loss from continuing operations	(802,285)	(488,126)
Discontinued operations, net of tax		13,804,517
Net income (loss)	(802,285)	13,316,391
Preferred stock dividend	(12,481)	(24,487)
Net income (loss) applicable to common shares	(814,766)	13,291,904
Other comprehensive income, net of tax effect of exchange rates (net of reclassification adjustments of \$0 and \$615,900)		(615,900)
Comprehensive income (loss)	\$ (814,766)	\$ 12,676,004
Basic and diluted weighted average common shares outstanding	10,578,974	9,121,094
Basic and diluted loss per common share for continuing operations	\$ (0.08)	\$ (0.06)
Basic and diluted income per common share for discontinued operations	\$	\$ 1.51
Basic and diluted income (loss) per common share	\$ (0.08)	\$ 1.46

See notes to unaudited consolidated financial statements.

TETON ENERGY CORPORATION

Unaudited Consolidated Statements of Operations and Comprehensive Income (Loss)

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	For the Nine Months Ended September 30,	
	2005	2004
Oil and gas sales	\$ 229,594	\$
Cost of sales and expenses:		
Lease operating expenses	3,000	
Production taxes	16,086	
General and administrative	3,045,691	4,350,594
Depletion, depreciation and amortization	84,231	7,315
Exploration	367,089	
Total cost of sales and expenses	3,516,097	4,357,909
Loss from operations	(3,286,503)	(4,357,909)
Other income		
Other income	184,018	70,460
Total other income	184,018	70,460
Loss from continuing operations	(3,102,485)	(4,287,449)
Discontinued operations, net of tax		13,101,338
Net income (loss)	(3,102,485)	8,813,889
Imputed preferred stock dividends for inducements and beneficial conversion charges		(521,482)
Preferred stock dividend	(61,456)	(81,462)
Net income (loss) applicable to common shares	(3,163,941)	8,210,945
Other comprehensive loss, net of tax effect of exchange rates (net of reclassification adjustments of \$0 and \$615,900)		(898,756)
Comprehensive income (loss)	\$ (3,163,941)	\$ 7,312,189
Basic and diluted weighted average common shares outstanding	9,954,057	8,996,498
Basic and diluted loss per common share for continuing operations	\$ (0.32)	\$ (0.54)
Basic and diluted income per common share for discontinued operations	\$	\$ 1.46
Basic and diluted income (loss) per common share	\$ (0.32)	\$ 0.91

See notes to unaudited consolidated financial statements.

TETON ENERGY CORPORATION

Unaudited Consolidated Statements of Cash Flows

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	For the Nine Months Ended September 30,	
	2005	2004
Cash flows from operating activities		
Net income(loss)	\$ (3,102,485)	\$ 8,813,889
Adjustments to reconcile net income (loss) to net cash used in operating activities		
Depreciation	84,231	7,315
Gain on sale of discontinued operations		(13,804,517)
Stock and warrants issued for services and interest	834,775	162,594
Changes in assets and liabilities		
From discontinued operations		1,740,268
Trade accounts receivable	(127,470)	
Prepaid expenses and other current assets	(83,725)	(96,387)
Accounts payable and accrued liabilities	(1,956)	55,176
Royalties and payroll taxes payable	117,385	
Advances to operator	(226,651)	
	596,589	(11,935,551)
Net cash used in operating activities	(2,505,896)	(3,121,662)
Cash flows from investing activities		
Proceeds from sale of discontinued operations net of taxes		7,933,450
Repayment of loans from discontinued operating entity		6,040,000
Increase in fixed assets	(5,372)	(28,421)
Increase in non-current of discontinued operating entity		(3,004,632)
Increase in oil and gas properties	(9,593,707)	
Decrease in other assets		
Net cash provided by (used in) investing activities	(9,599,079)	10,940,397
Cash flows from financing activities		
From discontinued operations		3,258,378
Proceeds from exercise of warrants and issuance of stock, net of issue costs of \$48,862 & \$50,000	2,702,209	499,999
Payment of dividends	(61,456)	(56,975)
Net cash provided by financing activities	2,640,753	3,701,402
Effect of exchange rates on cash and cash equivalents		(898,756)
Net increase (decrease) in cash and cash equivalents	(9,464,222)	10,621,381
Cash and cash equivalents - beginning of year	17,433,424	7,515,994
Cash and cash equivalents - end of period	\$ 7,969,202	\$ 18,137,375

See notes to unaudited consolidated financial statements.

TETON ENERGY CORPORATION

Unaudited Consolidated Statements of Cash Flows

Supplemental disclosure of non-cash activity:

During the nine months ended September 30, 2005, the Company had the following transactions:

The Company issued 12,828 shares of common stock to outside directors for settlement of accrued liabilities of \$10,500 at December 31, 2004.

The Company issued 281,460 shares of common stock upon the conversion of 281,460 shares of preferred stock.

The Company issued 450,000 shares of common stock, valued at \$837,000 and 200,000 warrants valued at \$251,949 in conjunction with a purchase of a 25% interest in Piceance Gas Resources, LLC.

The Company issued 412,962 shares of common stock valued at \$631,006, and 206,481 warrants valued at \$161,922, in conjunction with the purchase of acreage in the eastern Denver-Julesburg Basin.

The Company issued 287,500 shares to three consultants of the Company valued at \$905,625 for services, \$110,250 of which has been capitalized in oil and gas properties.

\$173,350 of capital expenditures are included in accounts payable at September 30, 2005.

The Company issued 10,776 shares of common stock valued at \$39,400 for services rendered by the outside directors.

The Company recorded an asset retirement obligation in the amount of \$2,543, with a corresponding increase to oil and gas properties.

During the nine months ended September 30, 2004, the Company had the following transactions:

100,000 warrants were issued to a consultant for services valued at \$102,094.

13,750 shares of common stock were issued for the settlement of accrued liabilities at December 31, 2003 valued at \$58,700.

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The Company issued (i) 1,306,669 non-qualified options to officers and directors valued at \$3,243,406; and (ii) 108,331 incentive stock options valued at \$268,899 with no expense being recorded for accounting purposes.

The Company issued 5,000 shares of common stock for services valued at \$20,000.

The Company (i) issued warrants valued at \$48,697 to consultants; (ii) issued 5,626 shares of common stock valued at \$23,329 to consultants; and (iii) issued 13,098 shares of common stock valued at \$46,000 for services rendered by the outside directors.

Approximately \$1,317,000 of capital expenditures for discontinued operations were included in accounts payable at June 30, 2004 and approximately \$1,786,000 of capital expenditures were in accounts payable at December 31, 2003 for a decrease during the six months ended June 30, 2004 of \$469,000.

The Company converted 463,207 shares of preferred stock, plus dividends of 37,057 shares, into 500,264 shares of common stock.

The Company issued 50,000 warrants valued at \$22,863 in settlement of accrued liabilities at December 31, 2003.

The Company accrued dividends to preferred stockholders of \$24,487 at September 30, 2004.

TETON ENERGY CORPORATION

Notes to Unaudited Consolidated Financial Statements

Note 1 - Basis of Presentation and Significant Accounting Policies

The September 30, 2005 financial statements are unaudited and reflect all adjustments (consisting only of normal recurring adjustments), which are, in the opinion of management, necessary for a fair presentation of the financial position and operating results for the interim periods. The financial statements include the accounts of the Company and its wholly owned subsidiaries. The Company consolidates its investment in Piceance Gas Resources, LLC, a Colorado limited liability company (Piceance LLC), using pro rata consolidation, whereby the Company has included its 25% pro rata share of Piceance LLC's assets, liabilities, revenues, expenses and oil and gas reserves in its financial statements. Prior to July 1, 2004 the unaudited financial statements also included a pro-rata consolidation of the Company's 35.3% interest in ZAO Goloil, a Russian closed joint-stock company (Goloil). The Company sold all of its interest in Goloil effective July 1, 2004 (See note 5). At the time of sale, Goloil's activities represented all of the oil and gas operating activities of the Company. As a result, the activities of Goloil have been reported as discontinued operations for all periods presented. The unaudited financial statements contained herein should be read in conjunction with the financial statements and notes thereto contained in the Company's financial statements for the year ended December 31, 2004, as reported in the Company's Form 10-K. The results of operations for the period ended September 30, 2005 are not necessarily indicative of the results for the entire fiscal year.

Note 2 - Earnings Per Share

All potential dilutive securities have an antidilutive effect on earnings (loss) per share and accordingly, basic and dilutive weighted average shares are the same.

Basic and diluted loss per common share from continuing operations includes the effects of preferred stock dividends.

Note 3 Stockholders' Equity

The terms of the certificate of designation for the Company's Preferred Stock include automatic conversion to Common Stock once the Company's Common Stock averaged \$6.00 per share for a period of 30 days. On September 23, 2005, the Company notified holders of its Series A Preferred Stock and its Series B Preferred Stock (the Preferred Stock) that their shares of Preferred Stock would be automatically converted into shares of the Company's Common Stock effective September 30, 2005, as such condition had been met.

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Also during the nine months ended September 30, 2005, 576,459 warrants were exercised, purchasing common shares of the Company for net proceeds to the Company of \$2,702,209.

On June 2, 2005, the Board of Directors of the Company declared a dividend distribution of one Preferred Stock Purchase Right (each a Right and collectively the Rights) for each outstanding share of Common Stock, \$0.001 par value (Common Stock), of the Company. The distribution was paid as of June 14, 2005 (the Record Date), to stockholders of record on that date. Each Right entitles the registered holder to purchase from the Company one one-hundredth of a share of the Company's Series C Preferred Stock, \$0.001 par value at a price of \$22.00, subject to adjustment on the occurrence of certain events which generally involve a person acquiring 15% of the Company's Common Stock without the permission of the Board of Directors. The description and terms of the Rights are set forth in the Rights Agreement dated as of June 3, 2005, between the Company and Computershare Investor Services, LLC, as Rights Agent.

Note 4 - Stock Options and Grants

During the first quarter of 2004, the Company issued 1,306,669 non-qualified stock options to employees, officers and directors valued at \$3,243,406 using the Black-Scholes option-pricing model with the following assumptions: volatility of 55.2%, a risk-free rate of 4%, zero dividend payments and a life of ten years. During the first quarter of 2004, the Company also issued 108,331 incentive stock options to employees, officers and directors valued at \$268,898 using the Black-Scholes option-pricing model under the same assumptions described above. These options were issued at an exercise price of \$3.60 per share and vested immediately. These options were issued pursuant to the Company's 2003 Employee Stock Compensation Plan (the 2003 Plan).

During the second quarter of 2005, the Company issued 45,000 stock options to various employees of the Company under the 2003 Plan. These options are exercisable at \$3.11 per share and vest over a three-year period, assuming the employees remain in the Company's employ. These stock options are valued at \$118,529 using the Black-Scholes option-pricing model with the following assumptions: volatility of 109.46%, a risk-free rate of 4%, zero dividend payments and a life of ten years. Beginning on January 1, 2006, when the Company adopts Statement of Financial Accounting Standards No. 123R, Share-Based Payment

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which is a revision of Statement of Financial Accounting Standards No. 123, *Accounting for Stock-Based Compensation*, the fair value of such shares will be recorded as an expense over the requisite service period for the employees.

On October 14, 2005, the Company filed a registration statement on Form S-8 registering the shares underlying options issued pursuant to the 2003 Plan.

At the Company's June 28, 2005 annual meeting the stockholders approved a Long Term Incentive Plan (the LTIP). The LTIP is a performance-based compensation plan whereby up to 10% of the outstanding shares at the beginning of each plan year, except for the first year wherein 20% of the outstanding shares are available (not to exceed, in any three year period, 35% of the outstanding shares of the Company) can be awarded to certain employees, directors and consultants. In most cases, awards will be linked to the performance of the Company as measured by performance metrics that, at the time of the grants, are deemed necessary by the Compensation Committee of the Board of Directors for the creation of shareholder value.

On July 26, 2005 the Compensation Committee finalized the award of 800,000 performance share units to the Company's Executive Officers and Directors. The performance share units are conditioned on the participants remaining employed by the Company, will vest over three years and will be awarded on a sliding scale from 50% to 200%, depending on the performance levels achieved by the Company.

At the annual meeting on July 16, 2004 the Company's shareholders approved a stock-based compensation plan for non-employees (the 2004 Plan). The maximum number of shares of Common Stock with respect to which awards can be granted is 1,000,000 shares. On April 5, 2005 the Board authorized the issuance of 140,000 restricted shares to the Company's Chief Financial Officer, 112,500 restricted shares to the Company's Legal Counsel and 35,000 restricted shares to a consultant providing land services on the Company's acquisitions. The shares were not formally issued to the consultants until the third quarter; however the Company recorded such shares at their fair value on April 5, 2005 of \$905,625 as if they were issued at June 30, 2005. The Company has capitalized \$110,250 of such amount and the balance of \$795,375 is included in 2005 general and administrative expenses.

Both the 2003 Plan and the 2004 Plan were terminated upon shareholder approval of the LTIP at the Company's 2005 annual meeting; however, grants made under these plans remain outstanding until exercised or terminated pursuant to each plan's terms.

The Company has adopted the disclosure-only provisions of Statement of Financial Accounting Standards No. 123, *Accounting for Stock-Based Compensation*. Accordingly, no compensation cost has been recognized for stock options issued to employees, officers and directors under the stock option plan. Had compensation cost for the Company's options issued to employees, officers and directors been determined based on the fair value at the grant date for awards consistent with the provisions of SFAS No. 123, as amended by SFAS No. 148, the Company's net income (loss) and basic income (loss) per common share would have been changed to the pro forma amounts indicated below:

	For the Three Months Ended September 30,	
	2005	2004
Net income (loss) applicable to common shares - as reported	\$ (814,766)	\$ 13,291,904
Add fair value of employee compensation expense	(9,877)	
Net income (loss) per common share - pro forma	\$ (824,643)	13,291,904

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Basic and diluted income(loss)per common share - as reported	\$	(0.08)	\$	1.46
Basic and diluted income(loss)per common share - pro forma	\$	(0.08)	\$	1.46

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	For the Nine Months Ended	
	September 30,	
	2005	2004
Net income (loss) applicable to common shares - as reported	\$ (3,163,941)	\$ 8,210,945
Add fair value of employee compensation expense	(9,877)	(3,512,305)
Net income (loss) per common share - pro forma	\$ (3,173,818)	\$ 4,698,640
Basic and diluted income(loss)per common share - as reported	\$ (0.32)	\$ 0.91
Basic and diluted income(loss)per common share - pro forma	\$ (0.32)	\$ 0.52