

Edgar Filing: ARENA RESOURCES INC - Form 10QSB

ARENA RESOURCES INC  
Form 10QSB  
May 15, 2003

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

FORM 10-QSB

(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, 2003

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 000-32439

ARENA RESOURCES, INC.  
-----

(Exact name of registrant as specified in its charter)

Nevada  
-----

73-1596109  
-----

(State or other jurisdiction of  
Incorporation or organization)

(I.R.S. Employer  
Identification No.)

4920 South Lewis Street, Suite 107  
Tulsa, Oklahoma 74105  
-----

(Address of principal executive officers)

(918) 747-6060  
-----

(Issuer's telephone number)

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 12, 2003, the Company had outstanding 6,382,856 shares of common stock (\$0.001 par value).

1

INDEX

Arena Resources, Inc.  
For the Quarter Ended March 31, 2003

Part I. Financial Information

Page

## Edgar Filing: ARENA RESOURCES INC - Form 10QSB

Item 1. Financial Statements (Unaudited)	3
Condensed Balance Sheets as of March 31, 2003 and December 31, 2002 (Unaudited)	4
Condensed Statements of Operations for the Three Months Ended March 31, 2003 and 2002 (Unaudited)	5
Condensed Statements of Cash Flows for the Three Months Ended March 31, 2003 and 2002 (Unaudited)	6
Notes to Condensed Financial Statements (Unaudited)	7
Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations	11
Item 3. Controls and Procedures	15
Part II. Other Information	
Item 1. Legal Proceedings	16
Item 4. Submission of Matters to a Vote of Security Holders	16
Item 5. Other Information	16
Item 6. Exhibits and Reports on Form 8-K	16
Signatures	17

2

### 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, 2003 are not necessarily indicative of the results to be expected for the year ending December 31, 2003.

3

ARENA RESOURCES, INC.  
CONDENSED BALANCE SHEETS  
(UNAUDITED)

Edgar Filing: ARENA RESOURCES INC - Form 10QSB

	March 31, 2003	December 31, 2002
-----		
ASSETS		
Current Assets		
Cash	\$ 1,216,320	\$ 796,915
Account receivable	274,890	269,436
Subscription receivable	-	157,500
Prepaid expenses	2,128	1,128
-----		
Total Current Assets	1,493,338	1,224,979
-----		
Property and Equipment, Using Full Cost Accounting		
Oil and gas properties subject to amortization	5,038,518	4,884,804
Equipment	21,794	21,794
Office equipment	14,672	14,672
-----		
Total Property and Equipment	5,074,984	4,921,270
Less: Accumulated depreciation and amortization	(222,477)	(172,258)
-----		
Net Property and Equipment	4,852,507	4,749,012
-----		
Long-Term Deposits	76,502	76,502
-----		
Total Assets	\$ 6,422,347	\$ 6,050,493
=====		
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities		
Accounts payable	\$ 94,292	\$ 173,174
Accrued liabilities	6,098	-
Accrued preferred dividends	68,301	114,685
-----		
Total Current Liabilities	168,691	287,859
-----		
Long-Term Liabilities		
Put option	45,828	50,604
Notes payable to officers	400,000	400,000
Deferred income taxes	303,593	187,193
-----		
Total Long-Term Liabilities	749,421	637,797
-----		
Stockholders' Equity		
Preferred stock - \$0.001 par value; 10,000,000 shares authorized; no shares issued or outstanding	-	-
Common stock - par value \$0.001 per share; 100,000,000 shares authorized; 6,372,856 shares and 6,282,056 shares outstanding, respect	6,373	6,282
Additional paid-in capital	5,418,902	5,287,189
Options and warrants outstanding	433,975	382,040
Accumulated deficit	(355,015)	(550,674)

Edgar Filing: ARENA RESOURCES INC - Form 10QSB

Total Stockholders' Equity	5,504,235	5,124,837
Total Liabilities and Stockholders' Equity	\$ 6,422,347	\$ 6,050,493

See accompanying notes to unaudited condensed financial statements.

4

ARENA RESOURCES, INC.  
CONDENSED STATEMENTS OF OPERATIONS  
(UNAUDITED)

For the Three Months Ended March 31	2003	2002
Oil and Gas Revenues	\$ 807,021	\$ 143,332
Costs and Operating Expenses		
Oil and gas production costs	242,071	46,556
Oil and gas production taxes	53,950	7,229
Depreciation, depletion and amortization	50,219	22,648
General and administrative expense	143,631	46,821
Total Costs and Operating Expenses	489,871	123,254
Other Income (Expense)		
Gain from change in fair value of put options	4,776	-
Interest expense	(9,867)	-
Net Other Expense	(5,091)	-
Income Before Provision for Income Taxes	312,059	20,078
Provision for Deferred Income Taxes	116,400	-
Net Income	195,659	20,078
Preferred Stock Dividends	-	39,706
Income (Loss) Attributable to Common Shares	\$ 195,659	\$ (19,628)

## Edgar Filing: ARENA RESOURCES INC - Form 10QSB

Basic Income (Loss) Per Common Share	\$ 0.03	\$ (0.01)
Diluted Income (Loss) Per Common Share	0.03	(0.01)
=====		
Basic Weighted-Average Common Shares Outstanding	6,327,609	3,604,500
Diluted Weighted-Average Common Shares Outstanding	6,327,609	3,604,500
=====		

See accompanying notes to unaudited condensed financial statements.

5

ARENA RESOURCES, INC.  
CONDENSED STATEMENTS OF CASH FLOWS  
(UNAUDITED)

For the Three Months Ended March 31	2003	2002
-----		
Cash Flows From Operating Activities		
Net income	\$ 195,659	\$ 20,078
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and depletion	50,219	22,648
Gain from change in fair value of put option	(4,776)	-
Changes in assets and liabilities:		
Accounts receivable	(5,454)	(24,822)
Prepaid expenses	(1,000)	-
Accounts payable and accrued liabilities	(72,784)	(6,496)
Deferred income taxes	116,400	-
-----		
Net Cash Provided by Operating Activities	278,264	11,408
-----		
Cash Flows from Investing Activities		
Purchase of oil and gas properties	(153,714)	(19,715)
Purchase of office equipment	-	(300)
Drilling advances	-	47,611
-----		
Net Cash Used in Investing Activities	(153,714)	27,596
-----		
Cash Flows From Financing Activities		
Proceeds from issuance of common stock, net of offering	183,739	-
Collection of common stock subscription receivable	157,500	-
Proceeds from issuance of preferred stock, net of offering costs	-	91,236
Payment on note payable	-	(8,000)
Payment of dividends to preferred stockholders	(46,384)	(36,144)
-----		
Net Cash Provided by Financing Activities	294,855	47,092
-----		
Net Increase in Cash	419,405	86,096

## Edgar Filing: ARENA RESOURCES INC - Form 10QSB

Cash at Beginning of Period	796,915	444,564
Cash at End of Period	\$1,216,320	\$530,660
Supplemental Cash Flows Information		
Cash paid for interest	\$ 9,867	\$ -

See accompanying notes to unaudited condensed financial statements.

6

ARENA RESOURCES, INC.  
NOTES TO UNAUDITED CONDENSED FINANCIAL STATEMENTS  
MARCH 31, 2003

NOTE 1 - 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, 2002. The financial position and results of operations for the three months ended March 31, 2003 are not necessarily indicative of the results to be expected for the full year ending December 31, 2003.

Nature of Operations - The Company owns interests in oil and gas properties located in Oklahoma, Texas and Kansas. 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.

Long-Term Deposits - The Company has complied with a requirement to maintain a \$50,000 certificate of deposit at a federally insured institution in order to do business in the state of Texas. The maturity date of the investment is July 2003. The Company has also complied with a requirement to maintain a \$25,000 certificate of deposit at a federally insured institution in order to do business in the state of Oklahoma. The maturity date of the investment is

## Edgar Filing: ARENA RESOURCES INC - Form 10QSB

August 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 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, 2003 was \$47,843 based on depletion at the rate of \$1.88 per barrel of oil equivalents compared to \$20,909 based on depletion at the rate of \$2.65 per barrel of oil equivalent for the three months ended March 31, 2002.

7

### ARENA RESOURCES, INC. NOTES TO UNAUDITED CONDENSED FINANCIAL STATEMENTS MARCH 31, 2003

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 (Loss) Per Common Share - Basic income (loss) per common share is computed by dividing net income (loss) available to common stockholders by the weighted-average number of common shares outstanding during the period. Diluted income (loss) per share reflects the potential dilution that could occur if all contracts to issue common stock were converted into common stock.

Concentration of Credit Risk and Major Customer - The Company currently has cash in excess of federally insured limits at March 31, 2003. During the three months ended March 31, 2003, sales to one customer represented 61% of total sales and sales to another customer represented 20% of total sales. At March 31, 2003, these two customers made up 57% and 19% of accounts receivable, respectively.

Stock-Based Employee Compensation - On April 1, 2003, the Company issued stock options to directors and employees, which are described more fully in Note 4. The Company applies the recognition and measurement principles of Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees (APB

## Edgar Filing: ARENA RESOURCES INC - Form 10QSB

25) and related interpretations in accounting for its stock-based compensation awards. Under APB 25, no compensation expense will be charged to earnings for employee stock option awards because the options granted had an exercise price equal to the fair value of the underlying common stock on the grant date.

Alternately, Statements on Financial Accounting Standards No. 123, Accounting for Stock-Based Compensation (SFAS 123), allows companies to recognize compensation expense over the related service period based on the grant date fair value of the stock option awards. Under both methods, upon issuance of common stock under the options, proceeds received in excess of par value are credited to additional paid-in capital. The dilutive effect of outstanding options is reflected as additional share dilution in the computation of income per common share. Although there was no effect on net income and income per share during the three months ended March 31, 2003 because the stock options were not granted during that period, future periods will include disclosure of the effect on net income and income per share as if the Company had applied the fair value recognition provisions of SFAS 123 to stock-based employee compensation. Under SFAS 123, the pro forma estimated compensation expense, after tax, for 2003, 2004 and 2005 will be approximately \$395,000, \$353,000 and \$209,000, respectively.

### NOTE 2 - 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. The interest rate is a floating rate equal to the JP Morgan Chase prime rate plus 1% with interest payable monthly. Annual fees for the facility are 1/2 of one percent of the unused portion of the borrowing base. Amounts borrowed under the revolving credit facility will be due in February 2005. 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 and the credit facility was guaranteed by two of the Company's officers. The Company is required under the terms of the credit facility to maintain a tangible net worth of \$4,000,000, maintain a 5-to-1 ratio

8

ARENA RESOURCES, INC.  
NOTES TO UNAUDITED CONDENSED FINANCIAL STATEMENTS  
MARCH 31, 2003

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. As of March 31, 2003, no amounts had been borrowed under this credit facility.

### NOTE 3 - STOCKHOLDERS' EQUITY

The Company is authorized to issue 100,000,000 common shares, with a par value of \$0.001 per share, and 10,000,000 Class "A" convertible preferred shares, with a par value of \$0.001 per share.

Private Placement Offering of Common Stock and Warrants - On August 22, 2002, the Company initiated a \$3,000,000 private placement offering of the Company's common stock at \$2.50 per share with a detachable warrant exercisable at \$5.00 per share through September 30, 2005. During the three months ended March 31, 2003, the Company issued 91,800 shares of common stock and 91,800 warrants for \$183,739 in net cash proceeds (net of cash offering costs of \$45,761). In



## Edgar Filing: ARENA RESOURCES INC - Form 10QSB

addition, the placement agents received, for their services, 16,830 warrants exercisable at \$5.00 per share through September 30, 2005. The net proceeds received were allocated to the common stock and the warrants based upon their relative fair values, with \$147,726 allocated to the common stock and \$36,013 allocated to the warrants. The fair value of the warrants issued was \$100,706, or \$0.93 per warrant, which was determined using the Black-Scholes option pricing model with the following weighted-average assumptions: risk-free interest rate of 1.8%, expected dividend yield of 0%, volatility of 35.7% and an expected life of 2.6 years.

In addition, during the three months ended March 31, 2003, the placement agents earned 52,433 additional warrants, with the same terms, for their services relating to the shares of common stock and warrants issued during 2002. During the three months ended March 31, 2003, \$15,922 of the proceeds from the 2002 cash offering proceeds were allocated to the additional warrants, based upon their relative fair value. Through March 31, 2003, the Company had issued 377,800 units of common stock and warrants to investors under the offering for \$785,875 in net cash proceeds (net of cash offering costs of \$158,625) and had issued 69,263 warrants to the placement agents for their services.

### NOTE 4 - EMPLOYEE STOCK OPTIONS

On April 1, 2003, the Company granted options to directors and employees to purchase 1,000,000 shares of common stock at \$3.70 per share through April 1, 2008, subject to shareholder approval. The options vest at the rate of 20% each year over five years. The exercise price was 85% of the market value of the Company's common stock on the date issued. In accordance with FASB Interpretation No. 44, Accounting for Certain Transactions Involving Stock Compensation, the 15% discount from the market price of the Company's common stock used in determining the fair value of the common stock is considered reasonable and the options are not compensatory. Accordingly, the Company will not recognize any compensation expense from the grant of these stock options in future periods.

The fair value of the options granted was \$1,837,935, or \$1.84 per share, and was estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted-average assumptions: dividend yield of 0% percent, expected volatility of 36.3%, risk-free interest rate of 2.8% and expected lives of 5.0 years.

9

ARENA RESOURCES, INC.  
NOTES TO UNAUDITED CONDENSED FINANCIAL STATEMENTS  
MARCH 31, 2003

### NOTE 5 - 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 and Oklahoma totaling \$75,000 to allow the Company to do business in those states. The standby letters of credit are valid through August 2004 and are collateralized by an assignment of certificates of deposit totaling \$76,502. 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 6 - SUBSEQUENT EVENTS

As discussed in Note 4, the Company granted stock options to directors and

## Edgar Filing: ARENA RESOURCES INC - Form 10QSB

employees on April 1, 2003 to purchase 1,000,000 shares of common stock at \$3.70 per share through April 1, 2008, subject to shareholder approval.

On April 15, 2003, the common stock of Arena Resources, Inc. began trading on the American Stock Exchange.

Effective May 1, 2003, Arena Resources, Inc. acquired a 70% working interest, 56% net revenue interest, in oil and gas properties known as the Seven Rivers Queen Unit in Lea County, New Mexico. Total consideration provided by the Company was a cash payment of \$900,000. These funds were drawn on the Company's revolving credit facility from the Bank of Oklahoma. The Company also issued 10,000 shares of the Company's common stock valued at \$4.50 per share, or \$45,000, as a finder's fee relating to this acquisition.

10

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

#### Results of Operations

For the three months ended March 31, 2003, the Company realized \$807,021 in revenue compared to \$143,332 in revenue for the same period in 2002. Income before accrual for deferred income taxes for the three months ended March 31, 2003 was \$312,059 compared to \$20,078 for the same period in 2002. Net income after preferred stock dividends was \$195,659 for the three months ended March 31, 2003 compared to a loss of \$19,628 for the same period in 2002. The Company also had positive net cash flows from operations of \$278,264, compared to \$11,408 for the same period in 2002.

Oil and gas production costs for the three months ended March 31, 2003 were \$242,071, compared to \$46,556 for the same period in 2002. Production taxes for the three months ended March 31, 2003 were \$53,950, compared to \$7,229 for the same period in 2002. Depreciation and depletion for the three months ended March 31, 2003 was \$50,219, compared to \$22,648 for the same period in 2002. General and administrative expenses for the three months ended March 31, 2003 were \$143,631, consisting primarily of bank line of credit fees, stock exchange listing fees and payroll salaries and taxes, compared to \$46,821 for the same period in 2002, consisting primarily of payroll salaries and taxes.

#### 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	5,440 BBLs	\$ 179,157
Oklahoma Leases	18,150 BBLs	\$ 579,882

##### GAS

	Net Production Volume	Net Revenue
Texas Leases	1,296 MCF	\$ 4,302
Oklahoma Leases	9,616 MCF	\$ 43,680

Arena is also looking at various other oil and gas opportunities, as generally outlined in its earlier periodic reports, in Oklahoma and other geographic

## Edgar Filing: ARENA RESOURCES INC - Form 10QSB

areas, but has entered no definitive or binding agreements, except as otherwise reported in this filing.

Significant Subsequent Events occurring after March 31, 2003:

On April 15, 2003, Arena Resources, Inc. common stock began trading on the American Stock Exchange, under ticker symbol ARD. The opening price was set at \$4.50 per share.

Effective May 1, 2003, Arena Resources, Inc. acquired a approximately 70% working interest, 56% net revenue interest, in the Seven Rivers Queen Unit in Lea County, New Mexico. Total consideration provided by the Company was a cash payment of \$900,000. The Company also issued 10,000 shares of the Company's restricted common stock valued at \$4.50 per share, or \$45,000, as a finder's fee relating to this acquisition.

11

### Capital Resources and Liquidity

As shown in the financial statements for the three months ended March 31, 2003, the Company had cash on hand of \$1,216,320, compared to \$792,915 as of December 31, 2002. The Company had positive net cash flows from operations for the three months ended March 31, 2003 of \$278,264, compared to \$11,408 for the same period 2002. Other significant sources of cash inflow in 2003 were the ongoing 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. Other significant sources of cash inflow in 2002 were the Class A preferred stock private placement (which closed June 30, 2002) with net proceeds of \$91,236, and drilling advances received of \$47,611. The most significant cash outflows during the three months ended March 31, 2003 and 2002 were capital expenditures of \$153,714 in 2003 and \$19,715 in 2002 and payment of preferred stock dividends of \$46,384 in 2003 and \$36,144 in 2002.

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. The interest rate is a floating rate equal to the JP Morgan Chase Prime rate plus 1% with interest payable monthly. Annual fees for the facility are 1/2 of 1% of the unused portion of the borrowing base. Amounts borrowed under the revolving credit facility will be due in February 2005. 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 and the credit facility was guaranteed by two of the Company's officers. The Company is required under the terms of the credit facility to maintain a tangible net worth of \$4,000,000, 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.

On August 22, 2002, the Company initiated a \$3,000,000 private placement offering of the Company's common stock at \$2.50 per share with a detachable warrant exercisable at \$5.00 per share through September 30, 2005. During the three months ended March 31, 2003, the Company issued 91,800 shares of common stock and 91,800 warrants for \$183,739 in net cash proceeds (net of cash offering costs of \$45,761). In addition, the placement agents received, for their services, 16,830 warrants exercisable at \$5.00 per share through September 30, 2005 and, during the three months ended March 31, 2003, the placement agents earned 52,433 additional warrants, with the same terms, for their services relating to the shares of common stock and warrants issued during 2002. Through March 31, 2003, the Company had issued 377,800 units of common stock and

## Edgar Filing: ARENA RESOURCES INC - Form 10QSB

warrants to investors under the offering for \$785,875 in net cash proceeds (net of cash offering costs of \$158,625) and had issued 69,263 warrants to the placement agents for their services.

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 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

12

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 and Oklahoma, 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 and Kansas specific oil and gas regulations exist related to the drilling, completion and operations of wells, as well as disposal of waste

## Edgar Filing: ARENA RESOURCES INC - Form 10QSB

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 or the Kansas Corporation Commission, Oil and Gas 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

13

statements. These statements speak only as of the date of this report. 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. 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.
- (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

## Edgar Filing: ARENA RESOURCES INC - Form 10QSB

financial officer.

14

### Part II - Other Information

#### Item 1. Legal Proceedings

Arena is not presently engaged in any legal proceedings, nor does it know of any claims for or against the company by any party.

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

During the present quarter there has been no matter submitted to security holders for a vote. Arena presently anticipates holding its first annual shareholders meeting in approximately the first half of 2003 for the election of directors, approval of its newly proposed stock option plan and the other routine matters, but has not presently set a definitive date for such meeting. Shareholders will be independently advised of any such formal annual meeting date.

#### Item 5. Other Information

Arena has established a limited trading market on the NASD Electronic Bulletin Board since approximately March 28, 2001. The shares have traded in the range of \$4.25 to \$4.50 during the first quarter, 2003 under the trading symbol, ARRI. As of April 15, 2003, Arena is trading on the American Stock Exchange under the trading symbol, ARD.

Arena discloses, as a material subsequent event, that it has rescinded and fully terminated its prior stock option program as of April 1, 2003. No shares were subscribed or issued under the terminated program. As of April 1, 2003, the Board adopted a new qualified stock option incentive plan, subject to shareholder approval as of the next shareholder meeting.

Management is not aware of any other pertinent or relevant information other than discussed above in Managements Discussion and Analysis of Financial Condition and Results of Operations. Shareholders are advised that as the Company completes future significant drilling and completion activities for oil and gas acquisitions that it will report such matters through press releases and/or the filing of 8-K reports where appropriate. Such information will be further summarized in the next applicable periodic filing with the Securities and Exchange Commission.

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

- (a) Exhibit 99 Certification Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant To Section 906 Of The Sarbanes-Oxley Act of 2002
- Exhibit 10.1 Seven Rivers Queen Unit Assignment, Bill of Sale and Conveyance dated May 1, 2003
- Exhibit 10.2 Form of Stock Option Subscription Agreements dated April 1, 2003

15

Edgar Filing: ARENA RESOURCES INC - Form 10QSB

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 14, 2003

By: /s/ Lloyd Tim Rochford  
-----

Lloyd Tim Rochford  
President, Chief Executive Officer

Dated: May 14, 2003

By: /s/ Stanley McCabe  
-----

Stanley McCabe  
Treasurer, Secretary

Dated: May 14, 2003

By: /s/ William R. Broaddrick  
-----

William R. Broaddrick  
Vice President, Chief Financial Officer

16

Attachment A

Form of Certification for Form 10-Q

CERTIFICATIONS

I, Lloyd Tim Rochford, certify that:

1. I have reviewed this quarterly report on Form 10-QSB of Arena Resources, Inc.;
2. Based on my knowledge, this quarterly report does not contain any untrue statement of 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

## Edgar Filing: ARENA RESOURCES INC - Form 10QSB

controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:

- a) designed such disclosure controls and procedures 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 function):

- 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.

Date: May 14, 2003

/s/ Lloyd Tim Rochford

---

Lloyd Tim Rochford  
President, Chief Executive Officer

I, William R. Broaddrick, certify that:

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



Edgar Filing: ARENA RESOURCES INC - Form 10QSB

2. Based on my knowledge, this quarterly report does not contain any untrue statement of 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 we have:
  - a) designed such disclosure controls and procedures 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 function):
  - 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
7. 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.

Date: May 14, 2003

Edgar Filing: ARENA RESOURCES INC - Form 10QSB

/s/ William R. Broaddrick

---

William R. Broaddrick  
Vice President, Chief Financial Officer