CONTINENTAL RESOURCES INC
Form S-1
March 07, 2006

Table of Contents

Index to Financial Statements

As filed with the Securities and Exchange Commission on March 7, 2006

Registration No. 333-

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM S-1

REGISTRATION STATEMENT

UNDER

THE SECURITIES ACT OF 1933

Continental Resources, Inc.

(Exact name of registrant as specified in charter)

Oklahoma	1311	73-0767549
(State or other jurisdiction of incorporation or organization)	(Primary Standard Industrial Classification Code Number)	(I.R.S. Employer Identification Number)

302 N. Independence

Enid, Oklahoma 73701

(580) 233-8955

(Address, including zip code, and telephone number, including area code, of registrant s principal executive offices)

Mark E. Monroe

President and Chief Operating Officer

302 N. Independence

Enid, Oklahoma 73701

(580) 233-8955

(Address, including zip code, and telephone number, including area code, of agent for service)

With a copy to:

David P. Oelman

Vinson & Elkins L.L.P.

1001 Fannin, Suite 2300

Houston, Texas 77002-6760

(713) 758-2222

Winthrop B. Conrad, Jr.

Davis Polk & Wardwell

450 Lexington Avenue

New York, New York 10017

(212) 450-4000

Approximate date of commencement of proposed sale to the public: As soon as practicable on or after the effective date of this Registration Statement.

If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, check the following box. ¨

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

CALCULATION OF REGISTRATION FEE

Title of Each Class of Securities to be Registered	Proposed Maximum Aggregate Offering Price	Amount of Registration Fee
Common stock, par value $.01	$ 575,000,000(1)(2)	$ 61,525

(1) Includes common stock issuable upon exercise of the underwriters option to purchase additional shares of common stock.
(2) Estimated solely for the purpose of calculating the registration fee pursuant to Rule 457(o).

The registrant hereby amends this registration statement on such date or dates as may be necessary to delay its effective date until the registrant shall file a further amendment which specifically states that this registration statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933 or until the registration statement shall become effective on such date as the Securities and Exchange Commission, acting pursuant to said Section 8(a), may determine.

Table of Contents

Index to Financial Statements

The information in this prospectus is not complete and may be changed. These securities may not be sold until the registration statement filed with the Securities and Exchange Commission is effective. This prospectus is not an offer to sell these securities nor does it seek an offer to buy these securities in any state where the offer or sale is not permitted.

Subject to completion, dated March 7, 2006

PROSPECTUS

Shares

Continental Resources, Inc.

Common Stock

This is our initial public offering of common stock. The selling shareholder identified in this prospectus is offering shares of our common stock. We will not receive any proceeds from the sale of the shares by the selling shareholder. The estimated initial public offering price is between $ and $ per share.

Prior to this offering, there has been no public market for our common stock. We intend to apply for listing of our common stock on the New York Stock Exchange under the symbol CXP.

Investing in our common stock involves a high degree of risk. See Risk factors beginning on page 13.

	Per share	**Total**

Initial public offering price	$	$
Underwriting discount	$	$
Proceeds to selling shareholder(1)	$	$

(1) Expenses, other than underwriting discounts, associated with the offering will be paid by us.

The selling shareholder has granted the underwriters an option for a period of 30 days to purchase up to additional shares of common stock to cover overallotments, if any.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or passed upon the adequacy or accuracy of this prospectus. Any representation to the contrary is a criminal offense.

The underwriters expect to deliver the shares of common stock to investors on , 2006.

JPMorgan **Merrill Lynch & Co.**

Citigroup

UBS Investment Bank

Petrie Parkman & Co.

Raymond James

, 2006

Table of Contents

Index to Financial Statements

[Map of Continental Resources, Inc. s areas of operations, including proved reserves per region, fourth quarter 2005 production, acreage and scheduled drilling locations.]

Table of Contents

Index to Financial Statements

Table of contents

	Page
Cautionary statement regarding forward-looking statements	ii
Industry and market data	iii
Prospectus summary	1
Risk factors	13
Use of proceeds	25
Dividend policy	25
Capitalization	26
Dilution	27
Selected historical and pro forma consolidated financial information	28
Management s discussion and analysis of financial condition and results of operations	32
Business and properties	51
Management	70
Selling shareholder and security ownership of certain beneficial owners and management	80
Certain relationships and related party transactions	81
Description of capital stock	85
Shares eligible for future sale	91
Material U.S. federal tax consequences for non-U.S. holders of our common stock	93
Underwriting	96
Legal matters	100
Experts	100
Where you can find more information	100
Index to audited historical consolidated financial statements	F-1
Glossary of oil and natural gas terms	A-1
Summary Report of Ryder Scott Company, L.P.	B-1

Table of Contents

Index to Financial Statements

Cautionary statement regarding forward-looking statements

This prospectus contains forward-looking statements that are subject to a number of risks and uncertainties, many of which are beyond our control. All statements, other than statements of historical fact included in this prospectus, regarding our strategy, future operations, financial position, estimated revenues and losses, projected costs, prospects, plans and objectives of management are forward-looking statements. When used in this prospectus, the words could, believe, anticipate, intend, estimate, expect, project and similar expressions are intended to identify forward-looking statements, although not all forward-looking statements contain such identifying words.

Forward-looking statements may include statements about our:

- business strategy;
- reserves;
- technology;
- financial strategy;
- oil and natural gas realized prices;
- timing and amount of future production of oil and natural gas;
- the amount, nature and timing of capital expenditures;
- drilling of wells;
- competition and government regulations;
- marketing of oil and natural gas;
- exploitation or property acquisitions;

costs of exploiting and developing our properties and conducting other operations;

general economic conditions;

uncertainty regarding our future operating results; and

plans, objectives, expectations and intentions contained in this prospectus that are not historical.

All forward-looking statements speak only as of the date of this prospectus. You should not place undue reliance on these forward-looking statements. Although we believe that our plans, intentions and expectations reflected in or suggested by the forward-looking statements we make in this prospectus are reasonable, we can give no assurance that these plans, intentions or expectations will be achieved. We disclose important factors that could cause our actual results to differ materially from our expectations under Risk factors and Management s discussion and analysis of financial condition and results of operations and elsewhere in this prospectus. These cautionary statements qualify all forward-looking statements attributable to us or persons acting on our behalf.

Table of Contents

Index to Financial Statements

Industry and market data

The market data and certain other statistical information used throughout this prospectus are based on independent industry publications, government publications or other published independent sources. Some data are also based on our good faith estimates. Although we believe these third-party sources are reliable, we have not independently verified the information and cannot guarantee its accuracy and completeness.

Table of Contents

Index to Financial Statements

Prospectus summary

This summary highlights information contained elsewhere in this prospectus. You should read this entire prospectus carefully, including Risk factors and our historical consolidated financial statements and the notes to those historical consolidated financial statements included elsewhere in this prospectus. Unless the context otherwise requires, references in this prospectus to Continental Resources, we, us, our, ours or company refer to Continental Resources, Inc. and its subsidiaries.

We have provided definitions for the oil and natural gas terms used in this prospectus in the Glossary of oil and natural gas terms beginning on page A-1 of this prospectus. Unless otherwise indicated, the information contained in this prospectus assumes that the underwriters do not exercise their option to purchase additional shares.

Our business

We are an independent oil and natural gas exploration and production company with operations in the Rocky Mountain, Mid-Continent and Gulf Coast regions of the United States. We focus our exploration activities in large new or developing plays that provide us the opportunity to acquire undeveloped acreage positions for future drilling operations. We have been successful in targeting large repeatable resource plays where horizontal drilling, advanced fracture stimulation and enhanced recovery technologies provide the means to economically develop and produce oil and natural gas reserves from unconventional formations. As a result of these efforts, we have grown substantially through the drillbit, adding 86.2 MMBoe of proved oil and natural gas reserves through extensions and discoveries from January 1, 2001 through December 31, 2005 compared to 4.7 MMBoe added through proved reserve purchases during that same period. These drillbit proved reserve additions replaced 309% of production during that period at an average drillbit finding cost of $5.89 per Boe.

As of December 31, 2005, our estimated proved reserves were 116.7 MMBoe, with a PV-10 of $2.2 billion. Our PV-10 and standardized measure of discounted future net cash flows are equivalent because we are a subchapter S-corporation. Estimated proved developed reserves were 80.3 MMBoe, or 69% of our total estimated proved reserves. Crude oil comprised 85% of our total estimated proved reserves. At December 31, 2005, we had 1,233 scheduled drilling locations on the 1,523,000 gross (961,000 net) acres that we held. For the year ended December 31, 2005, we generated revenues of $375.8 million and operating cash flows of $265.3 million.

Table of Contents

Index to Financial Statements

The following table summarizes our total estimated proved reserves, PV-10 and net producing wells as of December 31, 2005, average daily production for the three months then ended and the reserve-to-production ratio in our principal regions. Our reserve estimates as of December 31, 2005 are based primarily on a reserve report prepared by Ryder Scott Company, L.P., our independent reserve engineers. In preparing its report, Ryder Scott Company, L.P. evaluated properties representing approximately 83% of our PV-10. Our technical staff evaluated properties representing the remaining 17% of our PV-10.

	At December 31, 2005				Average daily production		
	Proved reserves (MBoe)	Percent of total	PV-10 (in millions)	Net producing wells	Fourth quarter 2005 (Boe per day)	Percent of total	Annualized reserve/ production index(1)
Rocky Mountain:							
Red River units	67,711	58%	$ 1,215	187	9,792	44%	18.9
Bakken field	23,878	21%	501	34	5,999	27%	10.9
Other	9,228	8%	141	230	1,694	8%	14.9
Mid-Continent	15,472	13%	328	630	3,715	17%	11.4
Gulf Coast	376		19	23	973	4%	1.1
Total	116,665	100%	$ 2,204	1,104	22,173	100%	14.4

(1) The Annualized Reserve/Production Index is the number of years proved reserves would last assuming current production continued at the same rate. This index is calculated by dividing annualized fourth quarter 2005 production into the proved reserve quantity at December 31, 2005.

The following table provides additional information regarding our key development areas:

	At December 31, 2005					2006 Budget	
	Developed acres		Undeveloped acres				Capital expenditures
	Gross	Net	Gross	Net	Scheduled drilling locations(1)	Wells planned for drilling	(in millions)
Rocky Mountain:							
Red River units	144,176	128,047			135	41	$ 84
Bakken field	52,421	38,971	588,081	356,426	918	54	96
Other	45,720	36,153	358,649	208,612	71	34	40
Mid-Continent	152,734	99,279	115,746	73,582	96	70	64
Gulf Coast	41,842	11,890	23,598	7,873	13	13	17

Total	436,893	314,340	1,086,074	646,493	1,233	212	$ 301

(1) Scheduled drilling locations represent total gross locations specifically identified and scheduled by management as an estimate of our future multi-year drilling activities on existing acreage. Of the total locations shown in the table, 256 are classified as PUDs. As of March 1, 2006, we have commenced drilling of 27 locations shown in the table, including 15 PUD locations. Scheduled drilling locations include 37 potential drilling sites in our New Albany Shale, Lewis Shale, Floyd Shale and Woodford Shale projects. While we own 168,000 gross (72,000 net) undeveloped acres in these projects, we have not sufficiently evaluated the opportunities on our acreage at this date to schedule further locations. Our actual drilling activities may change depending on oil and natural gas prices, the availability of capital, costs, drilling results, regulatory approvals and other factors. See Risk factors Risks relating to the oil and natural gas industry and our business.

Table of Contents

Index to Financial Statements

Our business strategy

Our goal is to increase shareholder value by finding and developing crude oil and natural gas reserves at costs that provide an attractive rate of return on our investment. The principal elements of our business strategy are:

Growth through low-cost drilling. Substantially all of our annual capital expenditures are invested in drilling projects and acreage and seismic acquisitions. From January 1, 2001 through December 31, 2005, proved oil and natural gas reserve additions through extensions and discoveries were 86.2 MMBoe compared to 4.7 MMBoe of proved reserve purchases. These drillbit proved reserve additions replaced 309% of production during that five-year period and 450% of production during 2005 at an average drillbit finding cost of $5.89 and $4.37 per Boe, respectively.

Internally generate prospects. Our technical staff internally generates substantially all of the opportunities for the investment of our capital. Because we are typically an early entrant in new or emerging plays, our costs to acquire undeveloped acreage are generally less than those of later entrants into a developing play. As an example of the cost advantage of entering a play early, our per acre costs for our lease acquisitions in the North Dakota Bakken field during 2003 and 2004 were approximately 80% lower than the per acre costs paid by third parties and by us in the federal and state lease auctions for acreage near our holdings in that area during 2005.

Focus on unconventional oil and natural gas resource plays. Our experience with horizontal drilling, advanced fracture stimulation and enhanced recovery technologies allows us to commercially develop unconventional oil and natural gas resource plays, such as the Red River B dolomite and Bakken Shale formations. Production rates in the Red River units also have been increased through the use of enhanced recovery technology. Our production from the Red River units and the Bakken field comprised approximately 71% of our total oil and natural gas production during the three months ended December 31, 2005.

Acquire significant acreage positions in new or developing plays. In addition to the 395,000 net acres held in the Montana and North Dakota Bakken field, we held 145,000 net acres in other oil and natural gas shale plays as of December 31, 2005. Our technical staff is focused on identifying and testing new unconventional oil and natural gas resource plays where significant reserves could be developed if commercial production rates can be achieved through advanced drilling, fracture stimulation and enhanced recovery techniques.

Our business strengths

We have a number of strengths that we believe will help us successfully execute our strategies:

Large drilling and acreage inventory. Within the Bakken field, we owned approximately 356,000 net undeveloped acres and had identified over 900 drilling locations as of December 31, 2005. We plan to allocate almost one-third of our current year capital expenditure budget towards developing our Bakken acreage position. Our large number of identified drilling locations provide for a multi-year drilling inventory and have the potential to make the Bakken field one of our largest sources of growth of reserves and production over the next several years.

Table of Contents

Index to Financial Statements

Within other unconventional plays such as the Lewis Shale in Wyoming, the Woodford Shale in Oklahoma, the New Albany Shale in Kentucky and Indiana and the Floyd Shale in Mississippi, we owned approximately 72,000 net undeveloped acres as of December 31, 2005. Within another resource play, the Pierre Shale in North Dakota and Montana, we have 56,000 net acres held by deeper production.

Additionally, at December 31, 2005, we owned approximately 218,000 net undeveloped acres in other projects, including 36,000 net undeveloped acres in Roosevelt County, Montana on which we are planning a 38-square mile 3-D seismic shoot in 2006, 31,000 net undeveloped acres in the Big Horn Basin in Wyoming on which we plan to drill four wells in 2006, 29,000 net undeveloped acres in Bowman County, North Dakota on which we are currently drilling a horizontal test well and 12,000 undeveloped net acres in Saskatchewan, Canada on which we plan to drill a horizontal test well in 2006.

Within the Red River units, we plan to drill 131 horizontal wells and 61 horizontal extensions of existing wellbores over the next two to three years in order to increase the density of both producing and injection wellbores. We believe these operations will significantly increase production and sweep efficiency. Production in the Red River units, as projected by our proved reserve report for the year ended December 31, 2005, is expected to peak in 2009 at approximately 19,000 net Boe per day. During the three months ended December 31, 2005, production in the Red River units averaged approximately 9,792 net Boe per day.

Horizontal drilling and enhanced recovery experience. In 1992, we drilled our initial horizontal well, and we have drilled over 300 horizontal wells since that time, which represented more than one-half of our total wells drilled during that period. We also have substantial experience with enhanced recovery methods and currently serve as the operator of 39 waterflood units. Additionally, we operate eight of the eleven high pressure air injection floods in the United States.

Control operations over a substantial portion of our assets and investments. As of December 31, 2005, we operated properties comprising 97% of our PV-10. By controlling operations, we are able to more effectively manage the cost and timing of exploration and development of our properties, including the drilling and fracture stimulation methods used. Our drillbit finding costs were $4.37 per Boe and $5.89 per Boe over the one- and five-year periods ending December 31, 2005, respectively.

Experienced management team. Our senior management team has extensive expertise in the oil and gas industry. Our Chief Executive Officer, Harold G. Hamm, began his career in the oil and gas industry in 1967. Our eight senior officers have an average of 25 years of oil and gas industry experience. Additionally, our technical staff, which includes 21 petroleum engineers, 14 geoscientists and seven landmen, has an average of more than 19 years experience in the industry.

Strong financial position. As of December 31, 2005, we had outstanding borrowings under our credit facility of approximately $143.0 million. We believe that our planned exploration and development activities will be funded substantially from our operating cash flows. As a result of our limited borrowings under our credit facility and strong operational cash flows, we did not enter into any oil or natural gas price hedges for our 2005 production, and we do not currently have any hedges in place.

Table of Contents

Index to Financial Statements

Risk factors

Investing in our common stock involves risks that include the speculative nature of oil and natural gas exploration, competition, volatile oil and natural gas prices and other material factors. You should read carefully the section entitled Risk Factors beginning on page 13 for an explanation of these risks before investing in our common stock. In particular, the following considerations may offset our business strengths or have a negative effect on our business strategy as well as on activities on our properties, which could cause a decrease in the price of our common stock and result in a loss of all or a portion of your investment:

A substantial or extended decline in oil and natural gas prices may adversely affect our business, financial condition or results of operations and our ability to meet our capital expenditure obligations and financial commitments.

Drilling for and producing oil and natural gas are high risk activities with many uncertainties that could adversely affect our business, financial condition or results of operations.

Reserve estimates depend on many assumptions that may turn out to be inaccurate. Any material inaccuracies in these reserve estimates or underlying assumptions will materially affect the quantities and present value of our reserves.

The results of enhanced recovery methods are uncertain.

Our development and exploitation projects require substantial capital expenditures. We may be unable to obtain needed capital or financing on satisfactory terms, which could lead to a decline in our oil and natural gas reserves.

If oil and natural gas prices decrease, we may be required to take write-downs of the carrying values of our oil and natural gas properties.

A substantial portion of our producing properties are located in the Rocky Mountains, making us vulnerable to risks associated with operating in one major geographic area.

Unless we replace our oil and natural gas reserves, our reserves and production will decline, which would adversely affect our cash flows and results of operations.

The unavailability or high cost of additional drilling rigs, equipment, supplies, personnel and oilfield services could adversely affect our ability to execute our exploration and development plans within our budget and on a timely basis.

We may incur substantial losses and be subject to substantial liability claims as a result of our oil and natural gas operations; we may not be insured for, or our insurance may be inadequate to protect us against, these risks.

Following this offering, our Chairman and Chief Executive Officer will own approximately % of our outstanding common stock, giving him influence and control in corporate transactions and other matters.

For a discussion of other considerations that could negatively affect us, including risks related to this offering and our common stock, see Risk factors and Cautionary statement regarding forward-looking statements.

Table of Contents

Index to Financial Statements

Corporate history and information

Continental Resources, Inc. is incorporated under the laws of the State of Oklahoma. We were originally formed in 1967 to explore, develop and produce oil and natural gas properties in Oklahoma. Through 1993, our activities and growth remained focused primarily in Oklahoma. In 1993, we expanded our activity into the Rocky Mountain and Gulf Coast regions. Through drilling success and strategic acquisitions, approximately 87% of our estimated proved reserves as of December 31, 2005 are located in the Rocky Mountain region.

Our principal executive offices are located at 302 N. Independence, Enid, Oklahoma 73701, and our telephone number at that address is (580) 233-8955.

Table of Contents

Index to Financial Statements

The offering

Common stock offered:

By the selling shareholder: shares

Common stock to be owned by the selling shareholder after the offering: shares

Common stock to be outstanding after the offering: shares

Use of proceeds:

We will not receive any proceeds from the sale of the shares of common stock by the selling shareholder. See Use of proceeds.

Dividend policy:

We do not anticipate paying any cash dividends on our common stock. See Dividend policy.

Proposed New York Stock Exchange symbol:

CXP

Other information about this prospectus:

Unless specifically stated otherwise, the information in this prospectus:

- is adjusted to reflect a for stock split of our shares of common stock to be effected in the form of a stock dividend prior to the consummation of this offering;
- assumes no exercise of the underwriters option to purchase additional shares; and
- assumes an initial public offering price of $, which is the mid-point of the range set forth on the front cover of this prospectus.

7

Table of Contents

Index to Financial Statements

Summary historical and pro forma consolidated financial data

This section presents our summary historical and pro forma consolidated financial data. The summary historical consolidated financial data presented below is not intended to replace our historical consolidated financial statements.

The following historical consolidated financial data, as it relates to each of the fiscal years ended December 31, 2001 through 2005, has been derived from our annual historical consolidated financial statements. You should read the following summary historical consolidated financial data in connection with Capitalization, Management s discussion and analysis of financial condition and results of operations and our audited historical consolidated financial statements and related notes included elsewhere in this prospectus. The summary historical consolidated results are not necessarily indicative of results to be expected in future periods.

The summary pro forma financial data reflect the tax effects of our conversion concurrent with the closing of this offering from a subchapter S-corporation to a subchapter C-corporation.

The share and per share information presented below does not give effect to the for stock split to be effected in the form of a stock dividend prior to the closing of this offering:

	Year ended December 31,				
(in thousands, except per share amounts)	**2001**	**2002**	**2003**	**2004**	**2005**
Statement of operations data:					
Revenues:					
Oil and natural gas sales	$ 112,170	$ 108,752	$ 138,948	$ 181,435	$ 361,833
Crude oil marketing and trading(1)	245,872	152,092	169,547	226,664	
Oil and natural gas service operations	6,047	5,739	9,114	10,811	13,931
Total revenues	364,089	266,583	317,609	418,910	375,764
Operating costs and expenses:					
Production expense	31,859	32,299	40,821	43,754	52,754
Production tax	8,385	7,729	10,251	12,297	16,031
Exploration expense	15,863	10,229	17,221	12,633	5,231
Crude oil marketing and trading(1)	245,003	152,718	166,731	227,210	
Oil and gas service operations	2,820	3,485	5,641	6,466	7,977
Depreciation, depletion, amortization and accretion	25,659	29,010	40,256	38,627	49,802
Property impairments	10,113	25,686	8,975	11,747	6,930
General and administrative	6,199	8,489	9,407	10,390	17,551
Equity compensation(2)		179	197	2,010	13,715
(Gain) loss on sale	(3,423)	(223)	(589)	150	(3,026)
Total operating costs and expenses	$ 342,478	$ 269,601	$ 298,911	$ 365,284	$ 166,965

8

Table of Contents

Index to Financial Statements

(in thousands, except per share amounts)	Year ended December 31, 2001	2002	2003	2004	2005
Income (loss) from operations	$ 21,611	$ (3,018)	$ 18,698	$ 53,626	$ 208,799
Other income (expense)					
Interest expense	(15,324)	(18,216)	(19,761)	(23,617)	(14,220)
Loss on redemption on bonds				(4,083)	
Other	645	912	295	890	867
Total other income (expense)	(14,679)	(17,304)	(19,466)	(26,810)	(13,353)
Income (loss) from continuing operations before income taxes	6,932	(20,322)	(768)	26,816	195,446
Provision for income taxes(3)					1,139
Income (loss) from continuing operations	6,932	(20,322)	(768)	26,816	194,307
Discontinued operations(4)	4,735	290	946	1,680	
Loss on sale of discontinued operations(4)				(632)	
Income (loss) before cumulative effect of change in accounting principle	11,667	(20,032)	178	27,864	194,307
Cumulative effect of change in accounting principle(5)			2,162		
Net income (loss)	$ 11,667	$ (20,032)	$ 2,340	$ 27,864	$ 194,307
Basic earnings (loss) per share:					
From continuing operations	$ 0.48	$ (1.41)	$ (0.05)	$ 1.87	$ 13.52
From discontinued operations(4)	0.33	0.02	0.06	0.11	
Loss on sale of discontinued operations(4)				(0.04)	
Before cumulative effect of change in accounting principle	0.81	(1.39)	0.01	1.94	13.52
Cumulative effect of change in accounting principle			0.15		
Net income (loss) per share	$ 0.81	$ (1.39)	$ 0.16	$ 1.94	$ 13.52
Shares used in basic earnings (loss) per share	14,369	14,369	14,369	14,369	14,369
Diluted earnings (loss) per share:					
From continuing operations	$ 0.48	$ (1.41)	$ (0.05)	$ 1.85	$ 13.42
From discontinued operations(4)	0.33	0.02	0.06	0.12	
Loss on sale of discontinued operations(4)				(0.04)	
Before cumulative effect of change in accounting principle	0.81	(1.39)	0.01	1.93	13.42
Cumulative effect of accounting change			0.15		
Net income (loss) per share	$ 0.81	$ (1.39)	$ 0.16	$ 1.93	$ 13.42
Shares used in diluted earnings (loss) per share	14,393	14,369	14,369	14,476	14,482

9

Table of Contents

Index to Financial Statements

	Year ended December 31,				
(in thousands, except per share amounts)	**2001**	**2002**	**2003**	**2004**	**2005**
Pro forma C-corporation data:					
Income (loss) from continuing operations before income taxes	$ 6,932	$ (20,322)	$ (768)	$ 26,816	$ 195,446
Pro forma provision (benefit) for income taxes attributable to operations	2,634	(7,722)	(292)	10,190	74,269
Pro forma income (loss) from operations after tax	4,298	(12,600)	(476)	16,626	121,177
Discontinued operations net of tax(4)	2,936	180	587	1,042	
Loss on sale of discontinued operations(4)				(392)	
Cumulative effect of change in accounting principal net of tax			1,340		
Pro forma net income (loss)	$ 7,234	$ (12,420)	$ 1,451	$ 17,276	$ 121,177
Pro forma net income (loss) per basic share	$ 0.50	$ (0.86)	$ 0.10	$ 1.20	$ 8.43
Pro forma net income (loss) per diluted share	0.50	(0.86)	0.10	1.19	8.37
Other financial data:					
Cash dividends per share	$	$	$	$ 1.04	$ 0.14
EBITDAX (6)	78,626	63,288	88,750	116,498	285,344
Net cash provided by operations	63,413	46,997	65,246	93,854	265,265
Net cash used in investing	(106,384)	(113,295)	(108,791)	(72,992)	(113,600)
Net cash provided by (used in) financing	43,045	61,593	43,302	(7,245)	(141,467)
Capital expenditures	111,023	113,447	114,145	94,307	144,800
Balance sheet data (at period end):					
Cash and cash equivalents	$ 7,225	$ 2,520	$ 2,277	$ 15,894	$ 6,014
Property and equipment, net	317,331	367,903	439,432	434,339	509,393
Total assets	354,485	406,677	484,988	504,951	600,234
Long-term debt, including current maturities	183,395	247,105	290,920	290,522	143,000
Shareholders equity	135,113	115,081	116,932	130,385	324,730

(1) Crude oil marketing and trading captions consist of our marketing activities under which crude oil production was sold at the wellhead and transported to a local hub where we purchased the barrels back to exchange at Cushing, Oklahoma in order to minimize pricing differentials with the NYMEX oil futures contract. We adopted Emerging Issues Task Force (EITF) 04-13 on January 1, 2005, which allowed certain purchase and sales transactions with the same counterparty to be combined and accounted for as a single transaction under the guidance of Accounting Principles Board Opinion No. 29. In 2005, we netted $39.8 million of crude oil marketing and trading revenues and $39.7 million of crude oil marketing and trading expenses under oil and natural gas sales. Prior to the adoption of EITF 04-13, we presented crude oil marketing and trading revenues and expenses gross under the guidance provided by EITF 99-19, Reporting Revenues Gross as a Principal and/or Net as an Agent. Effective March 2005, we ceased marketing our crude oil production under these arrangements. Thereafter, we have sold our crude oil at the wellhead. Certain of these sales have been to our affiliates, as described under Certain relationships and related party transactions.

(2) We have accounted for stock-based compensation under Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees using the intrinsic method. Our stock based compensation plan requires us to purchase vested shares at the employee s request based on an internally calculated fair-market value of our stock. Amounts in this caption represent

Table of Contents

Index to Financial Statements

the increase in our liability associated with our purchase obligation. The fair market valuation is based on the book value of our shareholders equity adjusted for our PV-10 as of each calendar quarter. Our requirement to purchase vested shares will be eliminated if we begin reporting under Section 12 of the Securities Exchange Act of 1934, as amended.

(3) Properties owned by us at May 31, 1997, the date we converted into a subchapter S-corporation from a subchapter C-corporation, may be subject to federal taxation if sold for an amount in excess of the difference between the conversion date fair market value and the then tax basis for the sold assets. During 2005, we incurred federal taxes due to the sale of assets acquired prior to May 31, 1997.

(4) In July 2004, we sold all of the outstanding stock in Continental Gas, Inc., a wholly owned subsidiary, to our shareholders. The Continental Gas, Inc. assets included seven gas gathering systems and three gas-processing plants. These assets represented our entire gas gathering, marketing and processing segment. We have accounted for these operations as discontinued operations.

(5) We adopted Statement of Financial Accounting Standards No. 143, Accounting for Asset Retirement Obligations and recorded the cumulative effect of the change in accounting principle on January 1, 2003.

(6) EBITDAX represents earnings before interest expense, income taxes (when applicable), depreciation, depletion, amortization and accretion, property impairments, exploration expense and non-cash compensation expense. EBITDAX is not a measure of net income or cash flow as determined by generally accepted accounting principles (GAAP). EBITDAX should not be considered as an alternative to, or more meaningful than, net income or cash flow as determined in accordance with GAAP or as an indicator of a company s operating performance or liquidity. Certain items excluded from EBITDAX are significant components in understanding and assessing a company s financial performance, such as a company s cost of capital and tax structure, as well as the historic costs of depreciable assets, none of which are components of EBITDAX. Our computations of EBITDAX may not be comparable to other similarly titled measures of other companies. We believe that EBITDAX is a widely followed measure of operating performance and may also be used by investors to measure our ability to meet future debt service requirements, if any. Our credit facility requires that we maintain a total debt to EBITDA ratio of no greater than 3.75 to 1 on a rolling four-quarter basis. Our credit facility defines EBITDA consistently with the definition of EBITDAX utilized and presented by us. At December 31, 2005, this ratio was approximately 0.5 to 1. The following table represents a reconciliation of our net income (loss) to EBITDAX:

	Year ended December 31,				
(in thousands)	**2001**	**2002**	**2003**	**2004**	**2005**
Net income (loss)	$ 11,667	$ (20,032)	$ 2,340	$ 27,864	$ 194,307
Interest expense	15,324	18,216	19,761	23,617	14,220
Provision for income taxes					1,139
Depreciation, depletion, amortization and accretion	25,659	29,010	40,256	38,627	49,802
Property impairments	10,113	25,686	8,975	11,747	6,930
Exploration expense	15,863	10,229	17,221	12,633	5,231
Equity compensation		179	197	2,010	13,715
EBITDAX	$ 78,626	$ 63,288	$ 88,750	$ 116,498	$ 285,344

Table of Contents

Index to Financial Statements

Summary reserve, production and operating data

The following table presents summary data with respect to our estimated net proved oil and natural gas reserves as of the dates indicated. Our reserve estimates as of December 31, 2003, 2004 and 2005 are based primarily on reserve reports prepared by Ryder Scott Company, L.P., our independent reserve engineers. In preparing its reports, Ryder Scott Company, L.P. evaluated properties representing approximately 83% of our PV-10 as of the end of each period. Our technical staff evaluated our remaining properties. A copy of Ryder Scott Company, L.P. s summary report as of December 31, 2005 is included in this prospectus beginning on page B-1. All calculations of estimated net proved reserves have been made in accordance with the rules and regulations of the Securities and Exchange Commission, or the SEC. For additional information regarding our reserves, see Business and properties Proved reserves.

	As of December 31,		
	2003	2004	2005
Proved reserves:			
Oil (MBbls)	73,000	80,602	98,645
Natural gas (MMcf)	67,096	60,620	108,118
Oil equivalent (MBoe)	84,183	90,705	116,665
Proved developed reserves percentage	55%	83%	69%
PV-10 (in millions)	$ 815	$ 1,114	$ 2,204
Estimated reserve life (in years)(1)	16.0	17.6	16.2
Costs incurred (in thousands):			
Property acquisition costs	$ 8,683	$ 12,456	$ 16,763
Exploration costs	11,981	30,867	9,289
Development costs	75,396	53,036	117,837
Total	$ 96,060	$ 96,359	$ 143,889
Annual drillbit reserve replacement percentage(2)	284%	155%	450%
Three-year average drillbit finding cost ($/Boe)			$ 6.01

(1) Calculated by dividing proved reserves by production volumes for the year indicated.

(2) Calculated by dividing reserve additions from extensions and discoveries by the production for the corresponding period.

The following table sets forth summary data with respect to our production results, average sales prices and production costs on a historical basis for the periods presented:

	Year ended December 31,		
	2003	2004	2005

Net production volumes:			
Oil (MBbls)	3,463	3,688	5,708
Natural gas (MMcf)	10,751	8,794	9,006
Oil equivalents (MBoe)	5,255	5,154	7,209
Average prices:			
Oil, without hedges ($/Bbl)	$ 28.88	$ 38.85	$ 52.45
Oil, with hedges ($/Bbl)	25.98	37.12	52.45
Natural gas ($/Mcf)	4.55	5.06	6.93
Oil equivalents, without hedges ($/Bbl)	28.35	36.45	50.19
Oil equivalents, with hedges ($/Bbl)	26.44	35.20	50.19
Costs and expenses:			
Production expense ($/Boe)	$ 7.77	$ 8.49	$ 7.32
Production tax ($/Boe)	1.95	2.39	2.22
General and administrative ($/Boe)	1.79	2.02	2.43
DD&A expense ($/Boe)	7.10	7.02	6.50

Table of Contents

Index to Financial Statements

Risk factors

You should carefully consider each of the risks described below, together with all of the other information contained in this prospectus, before deciding to invest in shares of our common stock. If any of the following risks develop into actual events, our business, financial condition or results of operations could be materially adversely affected, the trading price of your shares could decline and you may lose all or part of your investment.

Risks relating to the oil and natural gas industry and our business

A substantial or extended decline in oil and natural gas prices may adversely affect our business, financial condition or results of operations and our ability to meet our capital expenditure obligations and financial commitments.

The price we receive for our oil and natural gas production heavily influences our revenue, profitability, access to capital and future rate of growth. Oil and natural gas are commodities and, therefore, their prices are subject to wide fluctuations in response to relatively minor changes in supply and demand. Historically, the markets for oil and natural gas have been volatile. These markets will likely continue to be volatile in the future. The prices we receive for our production, and the levels of our production, depend on numerous factors beyond our control. These factors include the following:

- changes in global supply and demand for oil and natural gas;
- the actions of the Organization of Petroleum Exporting Countries, or OPEC;
- the price and quantity of imports of foreign oil and natural gas;
- political conditions in or affecting other oil-producing and natural gas-producing countries, including the current conflicts in the Middle East and conditions in South America and Russia;
- the level of global oil and natural gas exploration and production;
- the level of global oil and natural gas inventories;
- weather conditions;

technological advances affecting energy consumption; and

the price and availability of alternative fuels.

Lower oil and natural gas prices may also reduce the amount of oil and natural gas that we can produce economically. Substantial decreases in oil and natural gas prices would render uneconomic a significant portion of our exploitation projects. This may result in our having to make significant downward adjustments to our estimated proved reserves. As a result, a substantial or extended decline in oil or natural gas prices may materially and adversely affect our future business, financial condition, results of operations, liquidity or ability to finance planned capital expenditures.

Drilling for and producing oil and natural gas are high risk activities with many uncertainties that could adversely affect our business, financial condition or results of operations.

Our future success will depend on the success of our exploitation, exploration, development and production activities. Our oil and natural gas exploration and production activities are subject to

Table of Contents

Index to Financial Statements

numerous risks beyond our control, including the risk that drilling will not result in commercially viable oil or natural gas production. Our decisions to purchase, explore, develop or otherwise exploit prospects or properties will depend in part on the evaluation of data obtained through geophysical and geological analyses, production data and engineering studies, the results of which are often inconclusive or subject to varying interpretations. For a discussion of the uncertainty involved in these processes, see Reserve estimates depend on many assumptions that may turn out to be inaccurate. Any material inaccuracies in these reserve estimates or underlying assumptions will materially affect the quantities and present value of our reserves. Our cost of drilling, completing and operating wells is often uncertain before drilling commences. Overruns in budgeted expenditures are common risks that can make a particular project uneconomical. Further, many factors may curtail, delay or cancel drilling, including the following:

- delays imposed by or resulting from compliance with regulatory requirements;
- pressure or irregularities in geological formations;
- shortages of or delays in obtaining equipment and qualified personnel;
- equipment failures or accidents;
- adverse weather conditions, such as hurricanes and tropical storms;
- reductions in oil and natural gas prices;
- title problems; and
- limitations in the market for oil and natural gas.

Reserve estimates depend on many assumptions that may turn out to be inaccurate. Any material inaccuracies in these reserve estimates or underlying assumptions will materially affect the quantities and present value of our reserves.

The process of estimating oil and natural gas reserves is complex. It requires interpretations of available technical data and many assumptions, including assumptions relating to economic factors. Any significant inaccuracies in these interpretations or assumptions could materially affect the estimated quantities and present value of reserves shown in this prospectus. See Business and properties Proved reserves for information about our oil and natural gas reserves.

In order to prepare our estimates, we must project production rates and timing of development expenditures. We must also analyze available geological, geophysical, production and engineering data. The extent, quality and reliability of this data can vary. The process also requires economic assumptions about matters such as oil and natural gas prices, drilling and operating expenses, capital expenditures, taxes and availability of funds.

Actual future production, oil and natural gas prices, revenues, taxes, development expenditures, operating expenses and quantities of recoverable oil and natural gas reserves most likely will vary from our estimates. Any significant variance could materially affect the estimated quantities and present value of reserves shown in this prospectus. In addition, we may adjust estimates of proved reserves to reflect production history, results of exploration and development, prevailing oil and natural gas prices and other factors, many of which are beyond our control.

Table of Contents

Index to Financial Statements

You should not assume that the present value of future net revenues from our proved reserves referred to in this prospectus is the current market value of our estimated oil and natural gas reserves. In accordance with SEC requirements, we generally base the estimated discounted future net cash flows from our proved reserves on prices and costs on the date of the estimate. Actual future prices and costs may differ materially from those used in the present value estimate. If oil prices decline by $1.00 per Bbl, then our PV-10 as of December 31, 2005 would decrease from $2,204 million to $2,156 million. If natural gas prices decline by $0.10 per Mcf, then our PV-10 as of December 31, 2005 would decrease from $2,204 million to $2,199 million.

The results of enhanced recovery methods are uncertain.

We inject water and high-pressure air into formations on some of our properties to increase the production of oil and natural gas. The additional production and reserves attributable to the use of these enhanced recovery methods are inherently difficult to predict. If our enhanced recovery programs do not allow for the extraction of oil and natural gas in the manner or to the extent that we anticipate, our future results of operations and financial condition could be materially adversely affected.

Our development and exploitation projects require substantial capital expenditures. We may be unable to obtain needed capital or financing on satisfactory terms, which could lead to a decline in our oil and natural gas reserves.

The oil and natural gas industry is capital intensive. We make and expect to continue to make substantial capital expenditures in our business for the development, exploitation, production and acquisition of oil and natural gas reserves. To date, these capital expenditures have been financed with cash generated by operations and through borrowings from banks and from our principal shareholder. We intend to finance our future capital expenditures primarily through cash flow from operations and through borrowings under our revolving credit facility; however, our financing needs may require us to alter or increase our capitalization substantially through the issuance of debt or equity securities. The issuance of additional debt will require that a portion of our cash flow from operations be used for the payment of interest and principal on our debt, thereby reducing our ability to use cash flow to fund working capital, capital expenditures and acquisitions. The issuance of additional equity securities could have a dilutive effect on the value of your common stock.

Our cash flow from operations and access to capital are subject to a number of variables, including:

- our proved reserves;
- the level of oil and natural gas we are able to produce from existing wells;
- the prices at which our oil and natural gas are sold; and
- our ability to acquire, locate and produce new reserves.

If our revenues or the borrowing base under our credit facility decrease as a result of lower oil or natural gas prices, operating difficulties, declines in reserves or for any other reason, we may have limited ability to obtain the capital necessary to sustain our operations at current levels. If additional capital is needed, we may not be able to obtain debt or equity financing. If cash generated by operations or cash available under our revolving credit facility is not sufficient to meet our capital requirements, the failure to obtain additional financing could result in a

Table of Contents

Index to Financial Statements

curtailment of our operations relating to development of our prospects, which in turn could lead to a decline in our oil and natural gas reserves, and could adversely affect our business, financial condition and results of operations.

If oil and natural gas prices decrease, we may be required to take write-downs of the carrying values of our oil and natural gas properties.

Accounting rules require that we review periodically the carrying value of our oil and natural gas properties for possible impairment. Based on specific market factors and circumstances at the time of prospective impairment reviews, and the continuing evaluation of development plans, production data, economics and other factors, we may be required to write down the carrying value of our oil and natural gas properties. A write-down constitutes a non-cash charge to earnings. We may incur impairment charges in the future, which could have a material adverse effect on our results of operations for the periods in which such charges are taken.

A substantial portion of our producing properties are located in the Rocky Mountain region, making us vulnerable to risks associated with operating in one major geographic area.

Our producing properties are geographically concentrated in the Rocky Mountain region. In particular, a substantial portion of our proved reserves are located in the Red River units and in the Bakken field. At December 31, 2005, the Red River units and the Bakken field represented approximately 55% and 23% of our PV-10, respectively. As a result of this concentration, we may be disproportionately exposed to the impact of delays or interruptions of production from these wells caused by significant governmental regulation, transportation capacity constraints, curtailment of production or interruption of transportation of oil produced from the wells in these areas.

Unless we replace our oil and natural gas reserves, our reserves and production will decline, which would adversely affect our cash flows and results of operations.

Unless we conduct successful development, exploitation and exploration activities or acquire properties containing proved reserves, our proved reserves will decline as those reserves are produced. Producing oil and natural gas reservoirs generally are characterized by declining production rates that vary depending upon reservoir characteristics and other factors. Our future oil and natural gas reserves and production, and therefore our cash flow and results of operations, are highly dependent on our success in efficiently developing and exploiting our current reserves and economically finding or acquiring additional recoverable reserves. We may not be able to develop, exploit, find or acquire sufficient additional reserves to replace our current and future production.

The unavailability or high cost of additional drilling rigs, equipment, supplies, personnel and oilfield services could adversely affect our ability to execute our exploration and development plans within our budget and on a timely basis.

Shortages or the high cost of drilling rigs, equipment, supplies, personnel or oilfield services could delay or adversely affect our development and exploration operations, which could have a material adverse effect on our business, financial condition or results of operations.

16

Table of Contents

Index to Financial Statements

We may incur substantial losses and be subject to substantial liability claims as a result of our oil and natural gas operations; we may not be insured for, or our insurance may be inadequate to protect us against, these risks.

We are not insured against all risks. Losses and liabilities arising from uninsured and underinsured events could materially and adversely affect our business, financial condition or results of operations. Our oil and natural gas exploration and production activities are subject to all of the operating risks associated with drilling for and producing oil and natural gas, including the possibility of:

- environmental hazards, such as uncontrollable flows of oil, natural gas, brine, well fluids, toxic gas or other pollution into the environment, including groundwater and shoreline contamination;
- abnormally pressured formations;
- mechanical difficulties, such as stuck oilfield drilling and service tools and casing collapse;
- fires and explosions;
- personal injuries and death; and
- natural disasters.

Any of these risks could adversely affect our ability to conduct operations or result in substantial losses to our company as a result of:

- injury or loss of life;
- damage to and destruction of property, natural resources and equipment;
- pollution and other environmental damage;
- regulatory investigations and penalties;
- suspension of our operations; and
- repair and remediation costs.

We may elect not to obtain insurance if we believe that the cost of available insurance is excessive relative to the risks presented. In addition, pollution and environmental risks generally are not fully insurable. The occurrence of an event that is not fully covered by insurance could have a material adverse effect on our business, financial condition and results of operations.

Prospects that we decide to drill may not yield oil or natural gas in commercially viable quantities.

We describe some of our current prospects and our plans to explore those prospects in this prospectus. Our prospects are in various stages of evaluation, ranging from a prospect which is ready to drill to a prospect that will require substantial additional seismic data processing and interpretation. There is no way to predict in advance of drilling and testing whether any particular prospect will yield oil or natural gas in sufficient quantities to recover drilling or completion costs or to be economically viable. The use of seismic data and other technologies and the study of producing fields in the same area will not enable us to know conclusively prior

Table of Contents

Index to Financial Statements

to drilling whether oil or natural gas will be present or, if present, whether oil or natural gas will be present in commercial quantities. We cannot assure you that the analogies we draw from available data from other wells, more fully explored prospects or producing fields will be applicable to our drilling prospects.

Our identified drilling locations are scheduled out over several years, making them susceptible to uncertainties that could materially alter the occurrence or timing of their drilling.

Our management has specifically identified and scheduled drilling locations as an estimation of our future multi-year drilling activities on our existing acreage. As of December 31, 2005, we had identified and scheduled 1,233 gross drilling locations. These scheduled drilling locations represent a significant part of our growth strategy. Our ability to drill and develop these locations depends on a number of uncertainties, including oil and natural gas prices, the availability of capital, costs, drilling results, regulatory approvals and other factors. Because of these uncertainties, we do not know if the numerous potential drilling locations we have identified will ever be drilled or if we will be able to produce oil or natural gas from these or any other potential drilling locations. In addition, unless production is established within the spacing units covering the undeveloped acres on which some of the locations are identified, the leases for such acreage will expire. As of December 31, 2005, we had 93,922, 123,214 and 160,891 net acres expiring in 2006, 2007 and 2008, respectively. As such, our actual drilling activities may materially differ from those presently identified, which could adversely affect our business.

Market conditions or operational impediments may hinder our access to oil and natural gas markets or delay our production.

Market conditions or the unavailability of satisfactory oil and natural gas transportation arrangements may hinder our access to oil and natural gas markets or delay our production. The availability of a ready market for our oil and natural gas production depends on a number of factors, including the demand for and supply of oil and natural gas and the proximity of reserves to pipelines and terminal facilities. Our ability to market our production depends in substantial part on the availability and capacity of gathering systems, pipelines and processing facilities owned and operated by third parties. Our failure to obtain such services on acceptable terms could materially harm our business. We may be required to shut in wells due to lack of a market or inadequacy or unavailability of crude oil or natural gas pipeline or gathering system capacity. If that were to occur, then we would be unable to realize revenue from those wells until production arrangements were made to deliver to market.

We are subject to complex federal, state, local, provincial and other laws and regulations that could adversely affect the cost, manner or feasibility of conducting our operations.

Our oil and natural gas exploration, production and transportation operations are subject to complex and stringent laws and regulations. In order to conduct our operations in compliance with these laws and regulations, we must obtain and maintain numerous permits, approvals and certificates from various federal, state, local and provincial governmental authorities. We may incur substantial costs in order to maintain compliance with these existing laws and regulations. In addition, our costs of compliance may increase if existing laws and regulations are revised or reinterpreted, or if new laws and regulations become applicable to our operations. Such costs could have a material adverse effect on our business, financial condition and results of operations.

Our business is subject to federal, state, local and provincial laws and regulations as interpreted and enforced by governmental authorities possessing jurisdiction over various aspects of the

18

exploration for, and the production and transportation of, oil and natural gas. Failure to comply with such laws and regulations, as interpreted and enforced, could have a material adverse effect on our business, financial condition and results of operations. See Business and properties Environmental, health and safety regulation and Business and properties Regulation of the oil and natural gas industry for a description of the laws and regulations that affect us.

Our operations expose us to significant costs and liabilities with respect to environmental and operational safety matters.

We may incur significant costs and liabilities as a result of environmental, health and safety requirements applicable to our oil and natural gas exploration, production and transportation activities. These costs and liabilities could arise under a wide range of federal, state, local and provincial laws and regulations relating to protection of the environment, health and safety, including regulations and enforcement policies that have tended to become increasingly strict over time. Failure to comply with these laws and regulations may result in the assessment of administrative, civil and criminal penalties, imposition of cleanup and site restoration costs and liens, and, to a lesser extent, issuance of injunctions to limit or cease operations. In addition, claims for damages to persons or property, including natural resources, may result from the environmental, health and safety impacts of our operations.

Strict, joint and several liability may be imposed under certain environmental laws, which could cause us to become liable for the conduct of others or for consequences of our own actions that were in compliance with all applicable laws at the time those actions were taken. New laws, regulations or enforcement policies could be more stringent and impose unforeseen liabilities or significantly increase compliance costs. If we were not able to recover the resulting costs through insurance or increased revenues, our business, financial condition or results of operations could be adversely affected. See Business and properties Environmental, health and safety regulation for more information.

Competition in the oil and natural gas industry is intense.

We operate in a highly competitive environment for acquiring properties, marketing oil and natural gas and securing trained personnel. Many of our competitors possess and employ financial, technical and personnel resources substantially greater than ours, which can be particularly important in the areas in which we operate. Those companies may be able to pay more for productive oil and natural gas properties and exploratory prospects and to evaluate, bid for and purchase a greater number of properties and prospects than our financial or personnel resources permit. Our ability to acquire additional prospects and to find and develop reserves in the future will depend on our ability to evaluate and select suitable properties and to consummate transactions in a highly competitive environment. Also, there is substantial competition for capital available for investment in the oil and natural gas industry. We may not be able to compete successfully in the future in acquiring prospective reserves, developing reserves, marketing hydrocarbons, attracting and retaining quality personnel and raising additional capital.

The loss of senior management or technical personnel could adversely affect us.

To a large extent, we depend on the services of our senior management and technical personnel. The loss of the services of our senior management or technical personnel, including Harold G. Hamm, our Chairman and Chief Executive Officer, could have a material adverse effect on our operations. We do not maintain, nor do we plan to obtain, any insurance against the loss of any of

these individuals.

Table of Contents

Index to Financial Statements

Terrorist attacks aimed at our energy operations could adversely affect our business.

The continued threat of terrorism and the impact of military and other government action has led and may lead to further increased volatility in prices for oil and natural gas and could affect these commodity markets or financial markets used by us. In addition, the U.S. government has issued warnings that energy assets may be a future target of terrorist organizations. These developments have subjected our oil and natural gas operations to increased risks. Any future terrorist attack on our facilities, those of our customers and, in some cases, those of other energy companies, could have a material adverse effect on our business.

Seasonal weather conditions and lease stipulations adversely affect our ability to conduct drilling activities in some of the areas where we operate.

Oil and natural gas operations in the Rocky Mountains are adversely affected by seasonal weather conditions and lease stipulations designed to protect various wildlife. In certain areas, including parts of Montana, North Dakota, South Dakota, Utah and Wyoming, drilling and other oil and natural gas activities can only be conducted during the spring and summer months. This limits our ability to operate in those areas and can intensify competition during those months for drilling rigs, oilfield equipment, services, supplies and qualified personnel, which may lead to periodic shortages. These constraints and the resulting shortages or high costs could delay our operations and materially increase our operating and capital costs.

Our credit facility contains certain covenants that may inhibit our ability to make certain investments, incur additional indebtedness and engage in certain other transactions, which could adversely affect our ability to meet our future goals.

Our credit facility includes certain covenants that, among other things, restrict:

- our investments, loans and advances and the paying of dividends and other restricted payments;
- our incurrence of additional indebtedness;
- the granting of liens, other than liens created pursuant to the credit facility and certain permitted liens;
- mergers, consolidations and sales of all or substantial part of our business or properties;
- the hedging, forward sale or swap of our production of crude oil or natural gas or other commodities;
- the sale of assets; and

our capital expenditures.

Our credit facility requires us to maintain certain financial ratios, such as leverage ratios. All of these restrictive covenants may restrict our ability to expand or pursue our business strategies. Our ability to comply with these and other provisions of our credit facility may be impacted by changes in economic or business conditions, results of operations or events beyond our control. The breach of any of these covenants could result in a default under our credit facility, in which case, depending on the actions taken by the lenders thereunder or their successors or assignees, such lenders could elect to declare all amounts borrowed under our credit facility, together with accrued interest, to be due and payable. If we were unable to repay such borrowings or interest,

Table of Contents

Index to Financial Statements

our lenders could proceed against their collateral. If the indebtedness under our credit facility were to be accelerated, our assets may not be sufficient to repay in full such indebtedness.

The inability of our significant customers to meet their obligations to us may adversely affect our financial results.

We are subject to credit risk due to concentration of our crude oil and natural gas receivables with several significant customers. The three largest purchasers of our oil and natural gas in 2005 accounted for 31% , 19% and 10% of our total oil and natural gas sales revenues. We do not require our customers to post collateral. The inability of our significant customers to meet their obligations to us may adversely affect our financial results.

Risks relating to the offering and our common stock

The initial public offering price of our common stock may not be indicative of the market price of our common stock after this offering. In addition, our stock price may be volatile.

Prior to this offering, there has been no public market for our common stock. An active market for our common stock may not develop or may not be sustained after this offering. The initial public offering price of our common stock was determined by negotiations between us and representatives of the underwriters, based on numerous factors which we discuss in the Underwriting section of this prospectus. This price may not be indicative of the market price for our common stock after this initial public offering. The market price of our common stock could be subject to significant fluctuations after this offering, and may decline below the initial public offering price. You may not be able to resell your shares at or above the initial public offering price. The following factors could affect our stock price:

- our operating and financial performance and prospects;
- quarterly variations in the rate of growth of our financial indicators, such as net income per share, net income and revenues;
- changes in revenue or earnings estimates or publication of reports by equity research analysts;
- speculation in the press or investment community;
- sales of our common stock by us, Harold G. Hamm or other shareholders, or the perception that such sales may occur;

general market conditions, including fluctuations in commodity prices; and

domestic and international economic, legal and regulatory factors unrelated to our performance.

The stock markets in general have experienced extreme volatility that has often been unrelated to the operating performance of particular companies. These broad market fluctuations may adversely affect the trading price of our common stock.

Following this offering, our Chairman and Chief Executive Officer will own approximately % of our outstanding common stock, giving him influence and control in corporate transactions and other matters, including a sale of our company.

As of the closing of this offering, Harold G. Hamm, our Chairman and Chief Executive Officer, will beneficially own shares of our outstanding common stock, representing approximately % of

Table of Contents

Index to Financial Statements

our outstanding common stock. As a result, Mr. Hamm will continue to be our controlling shareholder and will continue to be able to control the election of our directors, determine our corporate and management policies and determine, without the consent of our other shareholders, the outcome of certain corporate transactions or other matters submitted to our shareholders for approval, including potential mergers or acquisitions, asset sales and other significant corporate transactions. As controlling shareholder, Mr. Hamm could cause, delay or prevent a change of control of our company. The interests of Mr. Hamm may not coincide with the interests of other holders of our common stock.

Several affiliated companies controlled by Mr. Hamm provide oilfield, gathering and processing, marketing and other services to us. We expect these transactions will continue in the future and may result in conflicts of interest between Mr. Hamm s affiliated companies and us. We can provide no assurance that any such conflicts will be resolved in our favor.

Purchasers of common stock in this offering will experience immediate and substantial dilution of $ per share.

Based on an assumed initial public offering price of $ per share, purchasers of our common stock in this offering will experience an immediate and substantial dilution of $ per share in the pro forma as adjusted net tangible book value per share of common stock from the initial public offering price, and our pro forma as adjusted net tangible book value as of December 31, 2005 after giving effect to this offering would be $ per share. See Dilution for a complete description of the calculation of net tangible book value.

The requirements of being a public company, including compliance with the reporting requirements of the Exchange Act and the requirements of the Sarbanes-Oxley Act, may strain our resources, increase our costs and distract management; and we may be unable to comply with these requirements in a timely or cost-effective manner.

As a public company with listed equity securities, we will need to comply with new laws, regulations and requirements, certain corporate governance provisions of the Sarbanes-Oxley Act of 2002, related regulations of the SEC and the requirements of the New York Stock Exchange (NYSE) with which we are not required to comply as a private company. Complying with these statutes, regulations and requirements will occupy a significant amount of time of our board of directors and management and will increase our costs and expenses. We will need to:

- institute a more comprehensive compliance function;
- design, establish, evaluate and maintain a system of internal controls over financial reporting in compliance with the requirements of Section 404 of the Sarbanes-Oxley Act of 2002 and the related rules and regulations of the SEC and the Public Company Accounting Oversight Board;
- comply with rules promulgated by the NYSE;
- prepare and distribute periodic public reports in compliance with our obligations under the federal securities laws;

establish new internal policies, such as those relating to disclosure controls and procedures and insider trading;

involve and retain to a greater degree outside counsel and accountants in the above activities; and

Table of Contents

Index to Financial Statements

establish an investor relations function.

In addition, we also expect that being a public company subject to these rules and regulations will require us to accept less director and officer liability insurance coverage than we desire or to incur substantial costs to obtain coverage. These factors could also make it more difficult for us to attract and retain qualified members of our board of directors, particularly to serve on our audit committee, and qualified executive officers.

Failure by us to achieve and maintain effective internal control over financial reporting in accordance with the rules of the SEC could harm our business and operating results and/or result in a loss of investor confidence in our financial reports, which could have a material adverse effect on our business and stock price.

We are in the process of evaluating our internal controls systems to allow management to report on, and our independent auditors to audit, our internal controls over financial reporting. We will be performing the system and process evaluation and testing (and any necessary remediation) required to comply with the management certification and auditor attestation requirements of Section 404 of the Sarbanes-Oxley Act of 2002. We will be required to comply with Section 404 for the year ending December 31, 2007. However, we cannot be certain as to the timing of completion of our evaluation, testing and remediation actions or the impact of the same on our operations. Furthermore, upon completion of this process, we may identify control deficiencies of varying degrees of severity under applicable SEC and Public Company Accounting Oversight Board rules and regulations that remain unremediated. As a public company, we will be required to report, among other things, control deficiencies that constitute a material weakness or changes in internal controls that, or that are reasonably likely to, materially affect internal controls over financial reporting. A material weakness is a significant deficiency or combination of significant deficiencies that results in more than a remote likelihood that a material misstatement of the annual or interim consolidated financial statements will not be prevented or detected. If we fail to implement the requirements of Section 404 in a timely manner, we might be subject to sanctions or investigation by regulatory authorities such as the SEC. In addition, failure to comply with Section 404 or the report by us of a material weakness may cause investors to lose confidence in our consolidated financial statements, and our stock price may be adversely affected as a result. If we fail to remedy any material weakness, our consolidated financial statements may be inaccurate, we may face restricted access to the capital markets and our stock price may be adversely affected.

We have no plans to pay dividends on our common stock, and therefore, you may not receive funds without selling your shares.

While we have declared a cash dividend of approximately $60.0 million payable to our shareholders for tax purposes and, subject to forfeiture, to holders of unvested restricted stock in April 2006, we do not anticipate paying any additional cash dividends on our common stock in the foreseeable future. We currently intend to retain future earnings, if any, to finance the expansion of our business. Our future dividend policy is within the discretion of our board of directors and will depend upon various factors, including our business, financial condition, results of operations, capital requirements and investment opportunities. In addition, our credit facility prohibits us from paying dividends other than for tax purposes.

Table of Contents

Index to Financial Statements

We are a controlled company within the meaning of NYSE rules and, as a result, we will qualify for, and may rely on, exemptions from certain corporate governance requirements.

Because Harold G. Hamm will beneficially own in excess of 50% of our outstanding shares of common stock after the completion of this offering, he will be able to control the composition of our board of directors and direct our management and policies. We also will be deemed to be a controlled company under the rules of the NYSE. Under these rules, we are not required to comply with certain corporate governance requirements of the NYSE, including:

- the requirement that a majority of our board of directors consist of independent directors;
- the requirement that we have a nominating/corporate governance committee that is composed entirely of independent directors with a written charter addressing the committee s purpose and responsibilities; and
- the requirement that we have a compensation committee that is composed entirely of independent directors with a written charter addressing the committee s purpose and responsibilities.

Following this offering, we may utilize some or all of these exemptions. Accordingly, you may not have the same protections afforded to shareholders of companies that are subject to all of the corporate governance requirements of the NYSE. Mr. Hamm s significant ownership interest could adversely affect investors perceptions of our corporate governance.

Provisions in our organizational documents and under Oklahoma law could delay or prevent a change in control of our company, which could adversely affect the price of our common stock.

We are an Oklahoma corporation. The existence of some provisions in our organizational documents, which we will amend and restate prior to the closing of this offering, and under Oklahoma law could delay or prevent a change in control of our company, which could adversely affect the price of our common stock. The provisions in our amended and restated certificate of incorporation and by-laws that could delay or prevent an unsolicited change in control of our company include a staggered board of directors, board authority to issue preferred stock and advance notice provisions for director nominations or business to be considered at a shareholder meeting. See Description of capital stock Anti-takeover effects of provisions of our certificate of incorporation and by-laws and of Oklahoma law.

Table of Contents

Index to Financial Statements

Use of proceeds

We will not receive any proceeds from the sale of the shares of common stock by the selling shareholder. We estimate that the selling shareholder will receive net proceeds of approximately $ million from the sale of the shares of our common stock in this offering based upon the assumed initial public offering price of $ per share, after deducting underwriting discounts and commissions. We will pay all expenses relating to the selling shareholder s sale of common stock in this offering, other than underwriting discounts and commissions. If the underwriters option to purchase additional shares is exercised in full, we estimate that the selling shareholder s net proceeds will be approximately $ million.

Dividend policy

Our credit facility prohibits us from paying dividends other than for tax purposes. As permitted by our credit facility, we have declared a cash dividend of approximately $60.0 million payable to our shareholders for tax purposes and, subject to forfeiture, to holders of unvested restricted stock in April 2006. In connection with the completion of this offering, we will convert from a subchapter S-corporation to a subchapter C-corporation, and we do not anticipate paying any additional cash dividends on our common stock in the foreseeable future. We currently intend to retain future earnings, if any, to finance the expansion of our business. Our future dividend policy is within the discretion of our board of directors and will depend upon various factors, including our results of operations, financial condition, capital requirements and investment opportunities.

Table of Contents

Index to Financial Statements

Capitalization

The following table shows our capitalization as of December 31, 2005:

on a historical basis, including the effect of a for stock split to be effected as a stock dividend prior to the consummation of this offering; and

on a pro forma basis to reflect our conversion, concurrent with the closing of this offering, from a subchapter S-corporation to a subchapter C-corporation, reclassification of equity compensation accruals and other transactions for which pro forma presentation is necessary in conjunction with this offering.

We derived this table from, and it should be read in conjunction with and is qualified in its entirety by reference to, the historical consolidated financial statements and the accompanying notes included elsewhere in this prospectus. You should read this information in conjunction with these consolidated financial statements and Management s discussion and analysis of financial condition and results of operations.

	As of December 31, 2005	
(in thousands)	**Historical**	**Pro forma**
Cash and cash equivalents	$ 6,014	$ 6,014
Long-term debt, including current maturities(1)	143,000	143,000
Shareholders equity:		
Common stock, $.01 par value; 20,000,000 shares authorized, 14,458,966 shares issued and outstanding actual and pro forma	144	144
Additional paid-in capital(2)	27,087	152,758
Retained earnings(1)(2)(3)	297,461	65,140
Accumulated other comprehensive loss, net of taxes	38	38
Total shareholders equity	324,730	218,080
Total capitalization	$ 467,730	$ 361,080

(1) We have declared a cash dividend of approximately $60.0 million payable to our shareholders for tax purposes and, subject to forfeiture, to holders of unvested restricted stock in April 2006. The payment of this dividend has not been included in retained earnings or long-term debt.

(2) Pro forma adjustments reflect reclassification of the liability for equity compensation of $12.2 million to additional paid-in capital, expensing offering costs of approximately $1.4 million, a charge to operations of approximately $117.4 million to recognize deferred taxes upon our conversion from a non-taxable subchapter S-corporation to a taxable subchapter C-corporation and reclassification of undistributed earnings

generated during the period of time we were organized as a subchapter S-corporation to additional paid-in capital in connection with our conversion to a subchapter C-corporation.

(3) Reflects a pro forma adjustment to recognize compensation expense for the increment between the fair market value at which compensation expense was recorded and the initial public offering price of $, the midpoint of the range set forth on the cover page of this prospectus.

26

Table of Contents

Index to Financial Statements

Dilution

Dilution is the amount by which the offering price paid by purchasers of common stock sold in this offering will exceed the net tangible book value per share of common stock after the offering. On a pro forma basis as of December 31, 2005, after giving effect to estimated offering expenses, our net tangible book value was $ million, or $ per share of common stock. Purchasers of common stock in this offering will experience substantial and immediate dilution in net tangible book value per share of common stock for financial accounting purposes, as illustrated in the following table:

Assumed initial public offering price per share		$
Net tangible book value per share as of December 31, 2005	$	
Decrease per share attributable to the offering	$	
Pro forma net tangible book value per share after the offering		$
Dilution in pro forma as adjusted net tangible book value per share to new investors		$

The following table sets forth, as of , 2006, the number of shares of common stock and the total consideration and average price per share paid by existing shareholders and by the new investors before deducting offering expenses:

	Shares acquired		Total consideration		Average price paid
	Number	**Percent**	**Amount**	**Percent**	**per share**
Existing shareholders			$ 27,231,000		
New investors					
Total					

27

Table of Contents

Index to Financial Statements

Selected historical and pro forma consolidated financial information

This section presents our selected historical and pro forma consolidated financial data. The selected historical consolidated financial data presented below is not intended to replace our historical consolidated financial statements.

The following historical consolidated financial data, as it relates to each of the fiscal years ended December 31, 2001 through 2005, has been derived from our annual historical consolidated financial statements. You should read the following selected historical consolidated financial data in connection with Capitalization, Management s discussion and analysis of financial condition and results of operations and our audited historical consolidated financial statements and related notes included elsewhere in this prospectus. The selected historical consolidated results are not necessarily indicative of results to be expected in future periods.

The selected pro forma financial data reflect the tax effects of our conversion concurrent with the closing of this offering from a subchapter S-corporation to a subchapter C-corporation.

The share and per share information presented below does not give effect to the for stock split to be effected in the form of a stock dividend prior to the closing of this offering:

	Year ended December 31,				
(in thousands, except per share amounts)	**2001**	**2002**	**2003**	**2004**	**2005**
Statement of operations data:					
Revenues:					
Oil and natural gas sales	$ 112,170	$ 108,752	$ 138,948	$ 181,435	$ 361,833
Crude oil marketing and trading(1)	245,872	152,092	169,547	226,664	
Oil and natural gas service operations	6,047	5,739	9,114	10,811	13,931
Total revenues	364,089	266,583	317,609	418,910	375,764
Operating costs and expenses:					
Production expense	31,859	32,299	40,821	43,754	52,754
Production tax	8,385	7,729	10,251	12,297	16,031
Exploration expense	15,863	10,229	17,221	12,633	5,231
Crude oil marketing and trading(1)	245,003	152,718	166,731	227,210	
Oil and gas service operations	2,820	3,485	5,641	6,466	7,977
Depreciation, depletion, amortization and accretion	25,659	29,010	40,256	38,627	49,802
Property impairments	10,113	25,686	8,975	11,747	6,930
General and administrative	6,199	8,489	9,407	10,390	17,551
Equity compensation(2)		179	197	2,010	13,715
(Gain) loss on sale	(3,423)	(223)	(589)	150	(3,026)

Total operating costs and expenses	$ 342,478	$ 269,601	$ 298,911	$ 365,284	$ 166,965

Table of Contents

Index to Financial Statements

(in thousands, except per share amounts)	Year ended December 31, 2001	2002	2003	2004	2005
Income (loss) from operations	$ 21,611	$ (3,018)	$ 18,698	$ 53,626	$ 208,799
Other income (expense)					
Interest expense	(15,324)	(18,216)	(19,761)	(23,617)	(14,220)
Loss on redemption on bonds				(4,083)	
Other	645	912	295	890	867
Total other income (expense)	(14,679)	(17,304)	(19,466)	(26,810)	(13,353)
Income (loss) from continuing operations before income taxes	6,932	(20,322)	(768)	26,816	195,446
Provision for income taxes(3)					1,139
Income (loss) from continuing operations	6,932	(20,322)	(768)	26,816	194,307
Discontinued operations(4)	4,735	290	946	1,680	
Loss on sale of discontinued operations(4)				(632)	
Income (loss) before cumulative effect of change in accounting principle	11,667	(20,032)	178	27,864	194,307
Cumulative effect of change in accounting principle(5)			2,162		
Net income (loss)	$ 11,667	$ (20,032)	$ 2,340	$ 27,864	$ 194,307
Basic earnings (loss) per share:					
From continuing operations	$ 0.48	$ (1.41)	$ (0.05)	$ 1.87	$ 13.52
From discontinued operations(4)	0.33	0.02	0.06	0.11	
Loss on sale of discontinued operations(4)				(0.04)	
Before cumulative effect of change in accounting principle	0.81	(1.39)	0.01	1.94	13.52
Cumulative effect of change in accounting principle			0.15		
Net income (loss) per share	$ 0.81	$ (1.39)	$ 0.16	$ 1.94	$ 13.52
Shares used in basic earnings (loss) per share	14,369	14,369	14,369	14,369	14,369
Diluted earnings (loss) per share:					
From continuing operations	$ 0.48	$ (1.41)	$ (0.05)	$ 1.85	$ 13.42
From discontinued operations(4)	0.33	0.02	0.06	0.12	
Loss on sale of discontinued operations(4)				(0.04)	
Before cumulative effect of change in accounting principle	0.81	(1.39)	0.01	1.93	13.42
Cumulative effect of accounting change			0.15		
Net income (loss) per share	$ 0.81	$ (1.39)	$ 0.16	$ 1.93	$ 13.42
Shares used in diluted earnings (loss) per share	14,393	14,369	14,369	14,476	14,482

29

Table of Contents

Index to Financial Statements

	Year ended December 31,				
(in thousands, except per share amounts)	2001	2002	2003	2004	2005
Pro forma C-corporation data:					
Income (loss) from continuing operations before income taxes	$ 6,932	$ (20,322)	$ (768)	$ 26,816	$ 195,446
Pro forma provision (benefit) for income taxes attributable to operations	2,634	(7,722)	(292)	10,190	74,269
Pro forma income (loss) from operations after tax	4,298	(12,600)	(476)	16,626	121,177
Discontinued operations net of tax(4)	2,936	180	587	1,042	
Loss on sale of discontinued operations(4)				(392)	
Cumulative effect of change in accounting principal net of tax			1,340		
Pro forma net income (loss)	$ 7,234	$ (12,420)	$ 1,451	$ 17,276	$ 121,177
Pro forma net income (loss) per basic share	$ 0.50	$ (0.86)	$ 0.10	$ 1.20	$ 8.43
Pro forma net income (loss) per diluted share	0.50	(0.86)	0.10	1.19	8.37
Other financial data:					
Cash dividends per share:	$	$	$	$ 1.04	$ 0.14
EBITDAX (6)	78,626	63,288	88,750	116,498	285,344
Net cash provided by operations	63,413	46,997	65,246	93,854	265,265
Net cash used in investing	(106,384)	(113,295)	(108,791)	(72,992)	(113,600)
Net cash provided by (used in) financing	43,045	61,593	43,302	(7,245)	(141,467)
Capital expenditures	111,023	113,447	114,145	94,307	144,800
Balance sheet data (at period end):					
Cash and cash equivalents	$ 7,225	$ 2,520	$ 2,277	$ 15,894	$ 6,014
Property and equipment, net	317,331	367,903	439,432	434,339	509,393
Total assets	354,485	406,677	484,988	504,951	600,234
Long-term debt, including current maturities	183,395	247,105	290,920	290,522	143,000
Shareholders equity	135,113	115,081	116,932	130,385	324,730

(1) Crude oil marketing and trading captions consist of our marketing activities under which crude oil production was sold at the wellhead and transported to a local hub where we purchased the barrels back to exchange at Cushing, Oklahoma in order to minimize pricing differentials with the NYMEX oil futures contract. We adopted Emerging Issues Task Force (EITF) 04-13 on January 1, 2005, which allowed certain purchase and sales transactions with the same counterparty to be combined and accounted for as a single transaction under the guidance of Accounting Principles Board Opinion No. 29. In 2005, we netted $39.8 million of crude oil marketing and trading revenues and $39.7 million of crude oil marketing and trading expenses under oil and natural gas sales. Prior to the adoption of EITF 04-13, we presented crude oil marketing and trading revenues and expenses gross under the guidance provided by EITF 99-19, Reporting Revenues Gross as a Principal and/or Net as an Agent. Effective March 2005, we ceased marketing our crude oil production under these arrangements. Thereafter, we have sold our crude oil at the wellhead. Certain of these sales have been to our affiliates, as described under Certain relationships and related party transactions.

(2) We have accounted for stock-based compensation under Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees using the intrinsic method. Our stock based compensation plan requires us to purchase vested shares at the employee s request based on an internally calculated fair-market value of our stock. Amounts in this caption represent the increase in our liability associated with our purchase obligation. The fair market valuation is based on the book value of our shareholders equity adjusted for our PV-10 as of each calendar quarter. Our requirement to purchase vested shares will be eliminated if we begin reporting under Section 12 of the Securities Exchange Act of 1934, as amended.

30

Table of Contents

Index to Financial Statements

(3) Properties owned by us at May 31, 1997, the date we converted into a subchapter S-corporation from a subchapter C-corporation, may be subject to federal taxation if sold for an amount in excess of the difference between the conversion date fair market value and the then tax basis for the sold assets. During 2005, we incurred federal taxes due to the sale of assets acquired prior to May 31, 1997.

(4) In July 2004, we sold all of the outstanding stock in Continental Gas, Inc., a wholly owned subsidiary, to our shareholders. The Continental Gas, Inc. assets included seven gas gathering systems and three gas-processing plants. These assets represented our entire gas gathering, marketing and processing segment. We have accounted for these operations as discontinued operations.

(5) We adopted Statement of Financial Accounting Standards No. 143, Accounting for Asset Retirement Obligations and recorded the cumulative effect of the change in accounting principle on January 1, 2003.

(6) EBITDAX represents earnings before interest expense, income taxes (when applicable), depreciation, depletion, amortization and accretion, property impairments, exploration expense and non-cash compensation expense. EBITDAX is not a measure of net income or cash flow as determined by generally accepted accounting principles (GAAP). EBITDAX should not be considered as an alternative to, or more meaningful than, net income or cash flow as determined in accordance with GAAP or as an indicator of a company s operating performance or liquidity. Certain items excluded from EBITDAX are significant components in understanding and assessing a company s financial performance, such as a company s cost of capital and tax structure, as well as the historic costs of depreciable assets, none of which are components of EBITDAX. Our computations of EBITDAX may not be comparable to other similarly titled measures of other companies. We believe that EBITDAX is a widely followed measure of operating performance and may also be used by investors to measure our ability to meet future debt service requirements, if any. Our credit facility requires that we maintain a total debt to EBITDA ratio of no greater than 3.75 to 1 on a rolling four-quarter basis. Our credit facility defines EBITDA consistently with the definition of EBITDAX utilized and presented by us. At December 31, 2005, this ratio was approximately 0.5 to 1. The following table represents a reconciliation of our net income (loss) to EBITDAX:

	Year ended December 31,				
(in thousands)	**2001**	**2002**	**2003**	**2004**	**2005**
Net income (loss)	$ 11,667	$ (20,032)	$ 2,340	$ 27,864	$ 194,307
Interest expense	15,324	18,216	19,761	23,617	14,220
Provision for income taxes					1,139
Depreciation, depletion, amortization and accretion	25,659	29,010	40,256	38,627	49,802
Property impairments	10,113	25,686	8,975	11,747	6,930
Exploration expense	15,863	10,229	17,221	12,633	5,231
Equity compensation		179	197	2,010	13,715
EBITDAX	$ 78,626	$ 63,288	$ 88,750	$ 116,498	$ 285,344

31

Table of Contents

Index to Financial Statements

Management s discussion and analysis of financial condition and results of operations

The following discussion should be read in conjunction with our historical consolidated financial statements and notes, as well as the selected historical consolidated financial data included elsewhere in this prospectus.

Overview

We are engaged in oil and natural gas exploration and exploitation activities in the Rocky Mountain, Mid-Continent and Gulf Coast regions of the United States. Crude oil comprised 85% of our 116.7 MMBoe of estimated proved reserves as of December 31, 2005 and 79% of our 7,209 MBoe of production for the year then ended. We seek to operate wells in which we own an interest, and we operated wells that accounted for 97% of our PV-10 and 1,213 of our 1,434 gross wells as of December 31, 2005. By controlling operations, we are able to more effectively manage the cost and timing of exploration and development of our properties, including the drilling and fracture stimulation methods used.

Our business strategy has focused on reserve and production growth through exploration and development. For the three-year period ended December 31, 2005, we added 55,385 MBoe of proved reserves through extensions and discoveries, compared to 426 MBoe added through purchases. During this period, our production increased from 5,255 MBoe in 2003 to 7,209 MBoe in 2005. An aspect of our business strategy has been to acquire large undeveloped acreage positions in new or developing locations. As of December 31, 2005, we held approximately 1,086,000 gross (646,000 net) undeveloped acres, including 356,000 net acres in the Bakken field in Montana and North Dakota and 72,000 net acres in the New Albany Shale, Lewis Shale, Floyd Shale and Woodford Shale projects. As an early entrant in new or emerging plays, our costs to acquire undeveloped acreage are generally less than those of later entrants into a developing play. As an example of the cost advantage of entering a play early, our per acre costs for our lease acquisitions in the North Dakota Bakken field during 2003 and 2004 were approximately 80% lower than the per acre costs paid by third parties and by us in the federal and state lease auctions for acreage near our holdings in that area during 2005. However, as an early entrant, we are exposed to the risk that the value of our undeveloped acreage is diminished by unsuccessful drilling results.

Our results of operations are determined primarily by three variables: (1) the volumes of oil and natural gas produced, (2) the prices realized for oil and natural gas sales, and (3) the success of our exploration and development drilling efforts. These performance measures, among others, are discussed below under How we evaluate our operations.

How we evaluate our operations

We use a variety of financial and operational measures to assess our performance. Among these measures are the following:

(1) Volumes of oil and natural gas produced;

(2) Oil and natural gas prices realized;

(3) Volumetric operating and administrative costs;

Table of Contents

Index to Financial Statements

(4) Reserve replacement ratio, finding cost and PV-10; and

(5) EBITDAX.

Volumes of oil and natural gas produced

For our operated properties in the Red River units and the Bakken field, we receive daily production estimates that enable us to monitor our production on a current basis. We believe the timeliness of this information and the control we exert as an operator enables us to respond promptly to production difficulties. Over the past three years our equivalent production volumes have increased 37% or 1,954 MBoe due primarily to a 65% increase in oil production. The following table presents our production volumes for each of the three years ended December 31, 2005:

				Three-year period	
	2003	2004	2005	Volume increase (decrease)	Percent increase (decrease)
MBbls	3,463	3,688	5,708	2,245	65%
MMcf	10,751	8,794	9,006	(1,745)	(16%)
MBoe	5,255	5,154	7,209	1,954	37%

The increase in our production has been the result of a favorable response to enhanced recovery efforts in our Red River units coupled with exploration and development within our other producing areas, primarily the Montana Bakken field.

Oil and natural gas prices realized

We market our oil and natural gas production to a variety of purchasers based on regional pricing. A significant portion of our oil and natural gas production has been marketed to affiliates as discussed under Certain relationships and related party transactions.

The following table presents the NYMEX oil and natural gas prices, our realized oil and natural gas prices, inclusive and exclusive of the effects of hedging, and the differences for each of the three years ended December 31, 2005. The NYMEX oil price was determined each month as the calendar month average of the prompt NYMEX crude oil futures contract price and, the NYMEX natural gas price, as the average of the last three trading days of the prompt NYMEX natural gas futures contract price. The

NYMEX natural gas futures contract price is quoted on an MMBtu basis. For purposes of comparison, in the table below the NYMEX natural gas price was converted to an Mcf basis at a one-to-one conversion:

	2003	2004	2005
NYMEX oil price ($/Bbl)	$ 31.08	$ 41.95	$ 57.69
Realized oil price before hedging ($/Bbl)	28.88	38.85	52.45
Difference	$ 2.20	$ 3.10	$ 5.24
NYMEX natural gas price ($/Mcf)	5.33	6.10	8.54
Realized natural gas price ($/Mcf)	4.55	5.06	6.93
Difference	$ 0.78	$ 1.04	$ 1.61

The differences are subject to variability due to quality and location pricing fluctuations caused by localized supply and demand fundamentals and transportation availability. In January 2006,

Table of Contents

Index to Financial Statements

the difference between the NYMEX oil price and our realized oil price was approximately $8 per Bbl and indications are that the difference may be between $10 and $11 per Bbl for February 2006. Factors affecting the difference include higher oil production in the region, lower demand by local refineries due to downtime for maintenance and reduced seasonal demand for gasoline and downstream transportation capacity constraints. We are unable to predict when, or if, the difference will revert back to historical levels.

Our revenues and net income are sensitive to oil and natural gas prices. A $1.00 per Bbl change in realized oil prices would change our reported 2005 revenues and net income by approximately $5.7 million and $5.4 million, respectively. Similarly, a $0.10 per Mcf change in realized natural gas prices would change our reported 2005 revenues and net income by approximately $901,000 and $852,000, respectively.

For the years ended December 31, 2003 and 2004, we realized oil hedging losses of $10.1 million and $6.4 million, respectively. As a result of our limited bank borrowings and strong operational cash flows, we did not enter into any hedges for our 2005 production, and we do not currently have any hedges in place.

Volumetric operating and administrative costs

Two other measures that we monitor and analyze are production expense per Boe produced and general and administrative expense per Boe produced. We believe these are important measures because they are indicators of operating cost efficiency.

The following table presents our production expense and general and administrative expense per Boe produced for each of the three years ended December 31, 2005:

	2003	2004	2005
Production expense ($/Boe)	$ 7.77	$ 8.49	$ 7.32
General and administrative expense ($/Boe)	1.79	2.02	2.43

Our per unit production expense increased during 2003 and 2004 in connection with our enhanced recovery project in the Red River units which initially lowered volumes and increased production expense. Our per unit production expense is now declining as we are experiencing higher production volumes due to continued drilling and favorable response to the enhanced recovery program. Generally as production increases, we will see increased production expense due to additional well costs, such as lifting and workover costs, and additional personnel costs although these costs may be lower on a volumetric basis due to higher production. General and administrative expense per Boe was $2.43 in 2005. We compete with other companies for personnel, particularly in the operational and technical (engineering and geologic) aspects of our business. To remain competitive, we compare the compensation we pay our employees to that of our competitors through surveys, employee feedback and other means. We have experienced higher compensation expense due to competitive pressures, normal merit increases and incentive compensation. Our incentive compensation has increased due to improving operating results. During 2004, we recorded incentive compensation of $413,000 compared to $4.0 million in 2005.

Reserve replacement ratio, finding cost and PV-10

Reserve replacement ratio, finding cost and PV-10 are three key measures against which we evaluate ourselves. Due to the depleting nature of oil and natural gas reserves, we seek to replace reserves produced and to grow our proved reserve quantity and value.

Table of Contents

Index to Financial Statements

The following table presents our reserve replacement ratio and finding cost for each of the three years ended December 31, 2005 and the PV-10 as of the end of each year:

	2003	2004	2005
Reserve replacement ratio from all sources	288%	227%	478%
Reserve replacement ratio from extensions and discoveries	284%	155%	450%
Finding cost per Boe using all sources	$ 6.34	$ 8.25	$ 4.18
Drillbit finding cost ($/Boe)	6.41	11.93	4.37
PV-10 (in millions)	815	1,114	2,204

Finding and developing oil and natural gas reserves economically is critical to our success. The reserve replacement ratio from all sources measures the degree to which we were able to replace production through exploration and development activities, revisions and proved reserve purchases. The finding cost per Boe using all sources was determined by dividing the costs incurred in proved and unproved property acquisitions and in exploration and development activities by the proved reserve Boe additions from extensions and discoveries, revisions and proved reserve purchases. The reserve replacement ratio from extensions and discoveries measures our ability to replace production through exploration and development activities.

Finding cost is a key metric that we utilize to evaluate the cost of additions to our reserve base. We believe we have been able to more effectively control the cost and timing of exploration and development of our properties, including the methods used, due to the high percentage of properties that we operate.

Ryder Scott Company, L.P. (Ryder Scott), our independent petroleum engineers, prepared an estimate of proved reserves for properties comprising approximately 83% of our PV-10 as of December 31, 2003, 2004 and 2005. Our technical staff evaluated the remaining properties. PV-10 is a valuation measure that is sensitive to changes in market prices. If oil prices decline by $1.00 per Bbl, then our PV-10 as of December 31, 2005 would decrease from $2,204 million to $2,156 million. If natural gas prices decline by $0.10 per Mcf, then our PV-10 as of December 31, 2005 would decrease from $2,204 million to $2,199 million. As a Subchapter S-corporation, we are not subject to federal or state corporate income taxes on our operating earnings because taxable income is passed through to our shareholders. As a result, our PV-10 and standardized measure of discounted future net cash flows are equivalent.

EBITDAX

We calculate and define EBITDAX as net income before interest expense, income taxes (when applicable), depreciation, depletion, amortization and accretion, property impairments, exploration expense and non-cash compensation expense. EBITDAX is used as a financial measure by our management team and by other users of our consolidated financial statements such as our commercial bank lenders, investors, research analysts and other to assess:

Our operating performance and return on capital in comparison to other independent exploration and production companies, without regard to financial or capital structure;

The financial performance of our assets and valuation of the entity without regard to financing methods, capital structure or historical cost basis; and

Our ability to generate cash sufficient to pay interest costs and support our indebtedness.

Table of Contents

Index to Financial Statements

The following table presents our EBITDAX for each of the three years ended December 31, 2005 (in thousands):

	2003	2004	2005
EBITDAX	$ 88,750	$ 116,498	$ 285,344

EBITDAX is a financial measure that is reported to our lenders each calendar quarter. Our credit facility requires that our total debt to EBITDA ratio be no greater that 3.75 to 1 on a rolling four quarter basis. This ratio was 0.5 to 1 at December 31, 2005. Our credit facility defines EBITDA consistently with the definition of EBITDAX utilized and presented by us. EBITDAX is not and should not be considered as an alternative to net income, operating income, cash flows from operating activities or any other measure of financial performance presented in accordance with GAAP. For a reconciliation of our consolidated net income (loss) to EBITDAX, see footnote (6) to Summary historical consolidated financial data.

Recent events

Our board of directors met on February 28, 2006 and declared the payment of a dividend of approximately $60.0 million ($ per share) for tax purposes to our existing shareholders and, subject to forfeiture, to holders of unvested restricted stock. This dividend will be paid on or about April 13, 2006.

Recognition of deferred taxes upon conversion to a subchapter C-corporation

Concurrent with the completion of this offering, we will convert from a subchapter S-corporation to a subchapter C-corporation. In connection with this conversion, a charge to earnings estimated to be approximately $117 million as of December 31, 2005 will be recorded to recognize deferred taxes.

Table of Contents

Index to Financial Statements

Results of operations

The following tables present selected financial and operating information for each of the three years ended December 31, 2005:

	Year ended December 31,		
(in thousands, except price data)	**2003**	**2004**	**2005**
Oil and natural gas sales	$ 138,948	$ 181,435	$ 361,833
Total revenues(1)	317,609	418,910	375,764
Operating costs and expenses(1)	298,911	365,284	166,965
Other income (expense)	(19,466)	(26,810)	(13,353)
Income (loss) from continuing operations before income taxes	(768)	26,816	195,446
Provision for income taxes			(1,139)
Income (loss) from continuing operations	(768)	26,816	194,307
Discontinued operations	946	1,680	
Loss on sale of discontinued operations		(632)	
Cumulative effect of a change in accounting principle	2,162		
Net income	$ 2,340	$ 27,864	$ 194,307
Production volumes:		&	