ZION OIL & GAS INC
Form 10-Q
May 08, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

MARK ONE

Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

for the Quarterly Period ended March 31, 2018; or

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

for the transition period from ________ to ________

ZION OIL & GAS, INC.

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	**20-0065053** (I.R.S. Employer Identification No.)
12655 N Central Expressway, Suite 1000, Dallas, TX (Address of principal executive offices)	**75243** Zip Code

(214) 221-4610

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company,” and “emerging growth company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer		Accelerated filer
Non-accelerated filer	(Do not check if a smaller reporting company)	Smaller reporting company
		Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

As of April 30, 2018, Zion Oil & Gas, Inc. had outstanding 58,021,582 shares of common stock, par value $0.01 per share.

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PART 1 – FINANCIAL INFORMATION

Zion Oil & Gas, Inc.

Balance Sheets as of (Unaudited)

	March 31, 2018 US$ thousands	December 31, 2017 US$ thousands
Current assets		
Cash and cash equivalents	4,770	6,892
Fixed short-term bank deposits – restricted	584	1,197
Prepaid expenses and other	432	434
Other deposits	533	540
Deferred offering costs	79	-
Governmental receivables	562	1,237
Other receivables	154	133
Total current assets	7,114	10,433
Unproved oil and gas properties, full cost method (see Note 4)	25,934	21,695
Property and equipment at cost		
Net of accumulated depreciation of $467 and $442	190	196
Other assets		
Fixed long-term bank deposits – restricted	991	990
Assets held for severance benefits	244	234
Total other assets	1,235	1,224
Total assets	34,473	33,548
Liabilities and Stockholders' Equity		
Current liabilities		
Accounts payable	1,890	2,750
Asset retirement obligation	470	470
Derivative liability (see Note 6)	5,400	1,866
Accrued liabilities	956	1,701
Total current liabilities	8,716	6,787
Long-term liabilities		
10% Senior convertible bonds, net of unamortized deferred financing cost of $84 and $90 and unamortized debt discount of $1,187 and $1,267 at March 31, 2018 and December 31, 2017 respectively (see Note 5)	2,015	2,002

Obligation under capital lease, net of current maturities of $10	37	39
Provision for severance pay	288	280
Total long-term liabilities	2,340	2,321
Total liabilities	11,056	9,108
Commitments and contingencies (see Note 7)		
Stockholders' equity		
Common stock, par value $.01; Authorized: 200,000,000 shares at March 31, 2018:		
Issued and outstanding: 57,344,379 and 55,888,399 shares at March 31, 2018 and December 31, 2017, respectively	573	559
Additional paid-in capital	189,699	184,485
Accumulated deficit	(166,855)	(160,604)
Total stockholders' equity	23,417	24,440
Total liabilities and stockholders' equity	34,473	33,548

The accompanying notes are an integral part of the unaudited interim financial statements.

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Zion Oil & Gas, Inc.

Statements of Operations (Unaudited)

	For the three months ended March 31, 2018 US$ thousands	2017 US$ thousands
General and administrative	1,959	2,847
Other	553	676
Loss from operations	(2,512)	(3,523)
Other income (expense), net		
(Loss) gain on derivative liability	(3,534)	273
Other income, net	-	10
Foreign exchange (loss) gain	(32)	31
Financial (expenses), net	(173)	(166)
Loss before income taxes	(6,251)	(3,375)
Income taxes	—	—
Net loss	(6,251)	(3,375)
Net loss per share of common stock - basic and diluted (in US$)	(0.11)	(0.07)
Weighted-average shares outstanding–basic and diluted (in thousands)	57,504	47,237

The accompanying notes are an integral part of the unaudited interim financial statements.

Zion Oil & Gas, Inc.

Statements of Changes in Stockholders' Equity (Unaudited)

	Common Stock		Additional paid-in	Accumulated	
	Shares	Amounts	Capital	deficit	Total
		US$	**US$**	**US$**	**US$**
	thousands	**thousands**	**thousands**	**thousands**	**thousands**
Balances as of December 31, 2017	55,888	559	184,485	(160,604)	24,440
Funds received from sale of DSPP units and shares	1,420	14	3,821	—	3,835
Value of bonds converted to shares	32	*	148	—	148
Funds received from option exercises	5	*	—	—	—
Value of options granted to employees, directors and others as non-cash compensation	—	—	1,245	—	1,245
Net loss	—	—	—	(6,251)	(6,251)
Balances as of March 31, 2018	57,345	573	189,699	(166,855)	23,417

The accompanying notes are an integral part of the unaudited interim financial statements.

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Zion Oil & Gas, Inc.

Statements of Cash Flows (Unaudited)

	For the three months ended March 31,	
	2018	2017
	US$ thousands	US$ thousands
Cash flows from operating activities		
Net loss	(6,251)	(3,375)
Adjustments required to reconcile net loss to net cash used in operating activities:		
Depreciation	14	10
Capital gain on sale of property and equipment	-	(10)
Cost of options issued to employees, directors and others as non-cash compensation	948	2,034
Interest and foreign exchange on short term and long term bank deposits	6	(17)
Amortization of debt discount related to convertible bonds	161	144
Change in derivative liability	3,534	(273)
Change in assets and liabilities, net:		
Other deposits	7	(264)
Prepaid expenses and other	2	(215)
Governmental receivables	675	(84)
Other receivables	(21)	1
Severance pay	(2)	(4)
Accounts payable	(108)	(116)
Accrued liabilities	50	(87)
Net cash used in operating activities	(985)	(2,256)
Cash flows from investing activities		
Redemption of short-term bank deposits	606	(503)
Investment in long-term bank deposits	-	(76)
Acquisition of property and equipment	(8)	(16)
Proceeds from sale of property and equipment	-	14
Investment in unproved oil and gas properties	(5,489)	(1,058)
Net cash used in investing activities	(4,891)	(1,639)
Cash flows from financing activities		
Deferred offering costs	(79)	-
Payments related to capital lease	(2)	(15)
Proceeds from sale of stock and exercise of options	3,835	4,580
Net cash provided by financing activities	3,754	4,565

Net (decrease) increase in cash, cash equivalents and restricted cash	(2,122)	670
Cash, cash equivalents and restricted cash – beginning of period	6,892	3,192
Cash, cash equivalents and restricted cash – end of period	4,770	3,862
Non-cash investing and financing activities:		
Cost of options capitalized to oil & gas properties	297	191
Unpaid investments in oil & gas properties	1,998	806
Subscription receivable for the sale of stock	-	650
10% Senior Convertible Bonds converted to shares	148	1
Acquisition of property and equipment under capital lease	-	71
Capitalized convertible bond interest attributed to oil and gas properties	86	-

The accompanying notes are an integral part of the unaudited interim financial statements.

Zion Oil & Gas, Inc.

Notes to Financial Statements (Unaudited)

Note 1 - Nature of Operations, Basis of Presentation and Going Concern

A. Nature of Operations

Zion Oil & Gas, Inc., a Delaware corporation ("we," "our," "Zion" or the "Company") is an oil and gas exploration company with a history of 18 years of oil & gas exploration in Israel. As of March 31, 2018, the Company has no revenues from its oil and gas operations.

Exploration Rights/Exploration Activities

The Company currently holds one active petroleum exploration license onshore Israel, the Megiddo-Jezreel License, comprising approximately 99,000 acres. The Megiddo Jezreel #1 ("MJ #1") site was completed in early March 2017, after which the drilling rig and associated equipment were mobilized to the site. Performance and endurance tests were completed, and the MJ #1 exploratory well was spud on June 5, 2017, ahead of the June 30, 2017 deadline under the then-existing license terms. The MJ #1 well has been drilled to a total depth ("TD") of 5,060 meters (approximately 16,600 feet). Thereafter, the Company obtained three open-hole wireline log suites (including a formation image log) and the well was successfully cased and cemented in preparation for upcoming testing of multiple zones of interest, including zone(s) where free-flowing hydrocarbons were collected after circulating mud in the borehole. After our review of the open-hole logs, we have finalized the testing program. The Ministry of Energy approved the well testing protocol on April 29, 2018. We have begun our testing program, and it may take several weeks to complete.

Depending on the final outcome and results of the active MJ #1 well and having adequate cash resources, multiple wells could be drilled from this pad site as several subsurface geologic targets are reachable using directional well trajectories.

Megiddo-Jezreel Petroleum License ("MJL")

The MJL was awarded on December 3, 2013 for a three-year primary term through December 2, 2016, with the possibility of additional one-year extensions up to an aggregate maximum of seven years. The MJL is onshore, south and west of the Sea of Galilee, and the Company continues its exploration focus here as it appears to possess the key geologic ingredients of an active petroleum system with significant exploration potential. In November of 2016, the State of Israel's Petroleum Commissioner officially approved the Company's drilling date and license extension request.

On October 30, 2017, the Company sought a multi-year extension to its existing license. After receiving feedback from Israel's Petroleum Commissioner, the Company submitted a revised extension request on November 9, 2017. On November 20, 2017, Israel's Petroleum Commissioner officially approved the Company's multi-year extension request on its Megiddo-Jezreel License No. 401, extending its validity to December 2, 2019. The Company now remains subject to the following updated key license terms:

Number	***Activity Description***	***Execution by:***
1	*Submit final report on the results of drilling*	*31 May 2018*
2	*Submit program for continuation of work under license*	*30 June 2018*

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Zion Oil & Gas, Inc.

Notes to Financial Statements

Note 1 - Nature of Operations, Basis of Presentation and Going Concern (cont'd)

As previously disclosed, the Company required authorization from the Israel Land Authority (the "ILA"), the formal lessor of the land to Kibbutz Sde Eliyahu, on whose property the drilling pad is currently situated, to access and utilize the drill site ("surface use agreement"). The Company received this authorization on July 4, 2016. This was preceded by the Company's May 15, 2016 signed agreement with the kibbutz. On January 11, 2017, an agreement was signed by the Company and the ILA by which the surface usage permission agreement was extended through December 3, 2017. On December 31, 2017, an agreement was signed by the Company and the ILA by which the surface usage permission agreement was extended through December 3, 2019.

Zion's Former Jordan Valley, Joseph, and Asher-Menashe Licenses

On March 29, 2015, the Energy Ministry formally approved the Company's application to merge the southernmost portion of the Jordan Valley License into the Megiddo-Jezreel License. The Company has plugged all of its exploratory wells (in the former Joseph and Asher-Menashe Licenses) but acknowledges its obligation to complete the abandonment of these well sites in accordance with guidance from the Environmental Ministry and local officials.

B. Basis of Presentation

The accompanying unaudited interim financial statements of Zion Oil & Gas, Inc. have been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") for interim financial information and with Article 8-03 of Regulation S-X. Accordingly, they do not include all of the information and notes required by GAAP for complete financial statements. In the opinion of management, all adjustments, consisting only of normal recurring accruals necessary for a fair statement of financial position, results of operations and cash flows, have been included. The information included in this Quarterly Report on Form 10-Q should be read in conjunction with the financial statements and the accompanying notes included in the Company's Annual Report on Form 10-K for the year ended December 31, 2017. The year-end balance sheet data presented for comparative purposes was derived from audited financial statements, but does not include all disclosures required by GAAP. The results of operations for the three months ended March 31, 2018 are not necessarily indicative of the operating results for the year ending December 31, 2018 or for any other subsequent interim period.

C. Going Concern

The Company incurs cash outflows from operations, and all exploration activities and overhead expenses to date have been financed by way of equity or debt financing. The recoverability of the costs incurred to date is uncertain and dependent upon achieving significant commercial production.

The Company's ability to continue as a going concern is dependent upon obtaining the necessary financing to undertake further exploration and development activities and ultimately generating profitable operations from its oil and natural gas interests in the future. The Company's current operations are dependent upon the adequacy of its current assets to meet its current expenditure requirements and the accuracy of management's estimates of those requirements. Should those estimates be materially incorrect, the Company's ability to continue as a going concern may be impaired. The financial statements have been prepared on a going concern basis, which contemplates realization of assets and liquidation of liabilities in the ordinary course of business. During the three months ended March 31, 2018, the Company incurred a net loss of approximately $6.2 million and had an accumulated deficit of approximately $167 million. These factors raise substantial doubt about the Company's ability to continue as a going concern.

To carry out planned operations, the Company must raise additional funds through additional equity and/or debt issuances or through profitable operations. There can be no assurance that this capital or positive operational income will be available to the Company, and if it is not, the Company may be forced to curtail or cease exploration and development activities. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

Zion Oil & Gas, Inc.

Notes to Financial Statements

Note 2 - Summary of Significant Accounting Policies

A. Net Loss per Share Data

Basic and diluted net loss per share of common stock, par value $0.01 per share (“Common Stock”), is presented in conformity with ASC 260-10 “Earnings Per Share.” Diluted net loss per share is the same as basic net loss per share, as the inclusion of 9,651,569 and 9,698,413 Common Stock equivalents in the three-month period ended March 31, 2018 and 2017 respectively, would be anti-dilutive.

B. Use of Estimates

The preparation of the accompanying financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions about future events. These estimates and the underlying assumptions affect the amounts of assets and liabilities reported, disclosures about contingent assets and liabilities, and reported amounts of revenues and expenses. Such estimates include the valuation of unproved oil and gas properties, deferred tax assets, asset retirement obligations and legal contingencies. These estimates and assumptions are based on management’s best estimates and judgment. Management evaluates its estimates and assumptions on an ongoing basis using historical experience and other factors, including the current economic environment, which management believes to be reasonable under the circumstances. The Company adjusts such estimates and assumptions when facts and circumstances dictate. Illiquid credit markets, volatile equity, foreign currency, and energy markets have combined to increase the uncertainty inherent in such estimates and assumptions. As future events and their effects cannot be determined with precision, actual results could differ significantly from these estimates. Changes in those estimates resulting from continuing changes in the economic environment will be reflected in the financial statements in future periods.

Zion Oil & Gas, Inc.

Notes to Financial Statements

Note 2 - Summary of Significant Accounting Policies (cont'd)

C. Oil and Gas Properties and Impairment

The Company follows the full-cost method of accounting for oil and gas properties. Accordingly, all costs associated with acquisition, exploration and development of oil and gas reserves, including directly related overhead costs, are capitalized.

All capitalized costs of oil and gas properties, including the estimated future costs to develop proved reserves, are amortized on the unit-of-production method using estimates of proved reserves. Investments in unproved properties and major development projects are not amortized until proved reserves associated with the projects can be determined or until impairment occurs. If the results of an assessment indicate that the properties are impaired, the amount of the impairment is included in loss from continuing operations before income taxes, and the adjusted carrying amount of the unproved properties is amortized on the unit-of-production method.

The Company's oil and gas property represents an investment in unproved properties. These costs are excluded from the amortized cost pool until proved reserves are found or until it is determined that the costs are impaired. All costs excluded are reviewed at least quarterly to determine if impairment has occurred. The amount of any impairment is charged to expense since a reserve base has not yet been established. Impairment requiring a charge to expense may be indicated through evaluation of drilling results, relinquishing drilling rights or other information.

During the three months ended March 31, 2018, and 2017, the Company did not record a non-cash impairment charge of its unproved oil and gas properties (see Note 4).

Currently, the Company has no economically recoverable reserves and no amortization base. The Company's unproved oil and gas properties consist of capitalized exploration costs of $25,934,000 and $21,695,000 as of March 31, 2018, and December 31, 2017, respectively.

D. Fair Value Measurements

The Company follows Accounting Standards Codification (ASC) 820, “Fair Value Measurements and Disclosures,” as amended by Financial Accounting Standards Board (FASB) Financial Staff Position (FSP) No. 157 and related guidance. Those provisions relate to the Company’s financial assets and liabilities carried at fair value and the fair value disclosures related to financial assets and liabilities. ASC 820 defines fair value, expands related disclosure requirements, and specifies a hierarchy of valuation techniques based on the nature of the inputs used to develop the fair value measures. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, assuming the transaction occurs in the principal or most advantageous market for that asset or liability.

There are three levels of inputs to fair value measurements - Level 1, meaning the use of quoted prices for identical instruments in active markets; Level 2, meaning the use of quoted prices for similar instruments in active markets or quoted prices for identical or similar instruments in markets that are not active or are directly or indirectly observable; and Level 3, meaning the use of unobservable inputs.

The Company uses Level 1 inputs for its fair value measurements whenever there is an active market, with actual quotes, market prices, and observable inputs on the measurement date. The Company uses Level 2 inputs for fair value measurements whenever there are quoted prices for similar securities in an active market or quoted prices for identical securities in an inactive market. The Company uses Level 3 inputs in the Binomial Model used for the valuation of the derivative liability.

Zion Oil & Gas, Inc.

Notes to Financial Statements

Note 2 - Summary of Significant Accounting Policies (cont'd)

E. Derivative Liabilities

In accordance with ASC 815-40-25 and ASC 815-10-15 Derivatives and Hedging and ASC 480-10-25 Liabilities-Distinguishing Liabilities from Equity, the embedded derivatives associated with the Convertible Bonds are accounted for as a liability during the term of the related Convertible Bonds (see Note 6).

F. Recently Adopted Accounting Pronouncements

In February 2016, the Financial Accounting Standards Board ("FASB") issued ASU 216-02, Leases (Topic 842) ("ASU 2016-02") in order to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet for those leases classified as operating leases under previous GAAP. ASU 2016-02 requires that a lessee should recognize a liability to make lease payments (the lease liability) and a right-of-use asset representing its right to use the underlying asset for the lease term on the balance sheet. ASU 2016-02 is effective for fiscal years beginning after December 15, 2018 (including interim periods within those periods) using a modified retrospective approach and early adoption is permitted. Zion will adopt ASU 2016-02 in the first quarter of 2019. Presently, Zion has operating leases for office space in Dallas, Texas and in Caesarea, Israel plus various leases for motor vehicles, among others. Those leases, and new leases entered in the future, will be accounted for under ASU 2016-02 in 2019 by establishing a right-of-use asset and a corresponding lease liability.

In November 2016, the FASB issued ASU 2016-18, Statement of Cash Flows (Topic 230) ("ASU 2016-18") to address the diversity that exists in the classification and presentation of restricted cash on the Statement of Cash Flows. The Company has adopted ASU 2016-18 and any applicable changes in the classification and presentation of restricted cash have been reflected in its Statement of Cash Flows.

Note 3 - Stockholders' Equity

A. 2011 Equity Incentive Stock Option Plan

During the three months ended March 31, 2018, the Company granted the following options from the 2011 Equity Incentive Plan for employees, directors and consultants, to purchase as non-cash compensation (the exercise of penny stock options are taxable on the date of exercise):

i. Options to purchase 330,000 shares of Common Stock to 23 senior officers, staff members and consultants at an exercise price of $.01 per share. The options have vesting schedules of 165,000 shares on June 30, 2018 and 165,000 shares on December 31, 2018. The options are exercisable through January 1, 2028. The fair value of the options at the date of grant amounted to approximately $759,000.

ii. Options to purchase 110,000 shares of Common Stock to five senior officers at an exercise price of $0.01 per share. The options vested upon grant and are exercisable through January 4, 2028. The fair value of the options at the date of grant amounted to approximately $250,000.

iii. Options to purchase 55,000 shares of Common Stock to three consultants an exercise price of $0.01 per share. The options vested upon grant. However, the exercisability of these options is according to the following schedule: (a) 27,500 options are exercisable on June 30, 2018 and (b) the remaining 27,500 options are exercisable on June 30, 2019. The fair value of the options at the date of grant amounted to $222,000.

B. 2011 Non-Employee Directors Stock Option Plan

During the three months ended March 31, 2018, the Company granted the following qualified (market value) options from the 2011 Non-Employee Directors Stock Option Plan for directors to purchase as non-cash compensation:

i. Options to purchase 400,000 shares of Common Stock to eight board members at an exercise price of $2.31 per share. The options vested upon grant and are exercisable through January 1, 2024. The fair value of the options at the date of grant amounted to approximately $428,000.

Zion Oil & Gas, Inc.

Notes to Financial Statements

Note 3 - Stockholders' Equity (cont'd)

C. Stock Options

The stock option transactions since January 1, 2018 are shown in the table below:

	Number of shares	**Weighted Average exercise price**
		US$
Outstanding, December 31, 2017	4,339,443	1.37
Changes during 2018 to:		
Granted to employees, officers, directors and others *	895,000	1.04
Expired/Cancelled/Forfeited	-	-
Exercised	(4,500)	0.01
Outstanding, March 31, 2018	5,229,943	1.31
Exercisable, March 31, 2018	4,824,943	1.42

* The receipt of a stock option grant by the grantee recipient is a non-taxable event according to the Internal Revenue Service. The grantee who later chooses to exercise penny stock options must recognize the market value in income in the year of exercise.

The following table summarizes information about stock options outstanding as of March 31, 2018:

Shares underlying outstanding options (fully vested)

Shares underlying outstanding options (non-vested)

Range of exercise price	Number outstanding	Weighted average remaining contractual life (years)	Weighted Average Exercise price	Range of exercise price	Number Outstanding	Weighted average remaining contractual life (years)	Weighted Average Exercise price
US$			US$	US$			US$
—	—	—	—	0.01	15,000	5.62	0.01
—	—	—	—	0.01	15,000	6.00	0.01
—	—	—	—	0.01	5,000	6.20	0.01
—	—	—	—	0.01	15,000	7.35	0.01
—	—	—	—	0.01	10,000	7.50	0.01
—	—	—	—	0.01	25,000	7.75	0.01
—	—	—	—	0.01	355,000	8.18	0.01
—	—	—	—	0.01	575,000	8.75	0.01
—	—	—	—	0.01	10,000	8.76	0.01
—	—	—	—	0.01	80,000	9.04	0.01
—	—	—	—	0.01	10,000	9.42	0.01
0.01	20,000	9.50	0.01	0.01	20,000	9.50	0.01
0.01	295,000	9.75	0.01	0.01	*35,000	9.75	0.01
—	—	—	—	0.01	**55,000	9.91	0.01
—	—	—	—	0.01	110,000	9.76	0.01
—	—	—	—	1.33	25,000	5.08	1.38
—	—	—	—	1.38	108,000	2.76	1.38
—	—	—	—	1.38	123,057	6.76	1.38
—	—	—	—	1.55	400,000	4.18	1.38
—	—	—	—	1.67	390,000	2.50	1.67
—	—	—	—	1.67	458,886	6.51	1.67
—	—	—	—	1.70	120,000	0.73	1.70
—	—	—	—	1.70	298,500	4.73	1.70
—	—	—	—	1.73	25,000	0.78	1.73
—	—	—	—	1.75	400,000	5.27	1.70
—	—	—	—	1.86	25,000	0.68	1.86
—	—	—	—	1.87	25,000	3.84	1.87
—	—	—	—	1.95	25,000	2.00	1.95
—	—	—	—	1.96	25,000	1.43	1.96
—	—	—	—	2.03	25,000	3.08	2.03
—	—	—	—	2.28	25,000	1.27	2.28
—	—	—	—	2.31	400,000	5.76	2.31
—	—	—	—	2.61	681,500	3.68	2.61
0.01	315,000		0.01	0.01-2.61	4,914,943		1.40

*17,500 options are exercisable on June 30, 2018 and 17,500 are exercisable on December 31, 2018.

**27,500 options are exercisable on June 30, 2018 and 27,500 are exercisable on June 30, 2019.

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Zion Oil & Gas, Inc.

Notes to Financial Statements

Note 3 - Stockholders' Equity (cont'd)

Granted to employees

The following table sets forth information about the weighted-average fair value of options granted to employees and directors during the year, using the Black Scholes option-pricing model and the weighted-average assumptions used for such grants:

	For the three months ended March 31,	
	2018	2017
Weighted-average fair value of underlying stock at grant date	**$2.31**	$1.37
Dividend yields	**—**	—
Expected volatility	**68%-70%**	60%
Risk-free interest rates	**2.01%-2.25%**	1.86%-1.93%
Expected lives (in years)	**3.50-5.50**	5.00
Weighted-average grant date fair value	**$1.69**	$1.36

Granted to non-employees

The following table sets forth information about the weighted-average fair value of options granted to non-employees during the year, using the Black Scholes option-pricing model and the weighted-average assumptions used for such grants:

	For the three months ended March 31,	
	2018	2017
Weighted-average fair value of underlying stock at grant date	**$3.37**	$1.36

Dividend yields	**—**	—
Expected volatility	**73%-76 %**	68 %
Risk-free interest rates	**2.46%-2.81 %**	2.36%-2.45%
Expected lives (in years)	**10.00**	10.00
Weighted-average grant date fair value	**$3.36**	$1.36

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Zion Oil & Gas, Inc.

Notes to Financial Statements

Note 3 - Stockholders' Equity (cont'd)

The risk-free interest rate is based on the U.S. Treasury yield curve in effect at the time of grant for periods corresponding with the expected life of the options.

The expected life represents the weighted average period of time that options granted are expected to be outstanding. The expected life of the options granted to employees and directors is calculated based on the Simplified Method as allowed under Staff Accounting Bulletin No. 110 ("SAB 110"), giving consideration to the contractual term of the options and their vesting schedules, as the Company does not have sufficient historical exercise data at this time. The expected life of the option granted to non-employees equals their contractual term. In the case of an extension of the option life, the calculation was made on the basis of the extended life.

D. Compensation Cost for Warrant and Option Issuances

The following table sets forth information about the compensation cost of warrant and option issuances recognized for employees and directors:

For the three months ended March 31,	
2018	**2017**
US$ thousands	**US$ thousands**
943	2,015

The following table sets forth information about the compensation cost of warrant and option issuances recognized for non-employees:

For the three months ended March 31,	
2018	**2017**
US$ thousands	**US$ thousands**
302	210

The following table sets forth information about the compensation cost of option issuances recognized for employees and non-employees and capitalized to Unproved Oil & Gas properties:

For the three months ended March 31,	
2018	**2017**
US$ thousands	**US$ thousands**
297	191

As of March 31, 2018, there was approximately $465,000 of unrecognized compensation cost, related to non-vested stock options granted under the Company's various stock option plans. The cost is expected to be recognized during the years 2018 and 2019.

E. Dividend Reinvestment and Stock Purchase Plan ("DSPP")

On March 27, 2014, the Company launched its Dividend Reinvestment and Stock Purchase Plan (the "DSPP") pursuant to which stockholders and interested investors can purchase shares of the Company's Common Stock as well as units of the Company's securities. The terms of the DSPP are described in the Prospectus Supplement originally filed on March 31, 2014 (the "Original Prospectus Supplement") with the Securities and Exchange Commission ("SEC") under the Company's effective registration Statement on Form S-3, as thereafter amended.

On January 13, 2015, the Company amended the Original Prospectus Supplement (“Amendment No. 3”) to provide for a unit option (the “Unit Option”) under the DSPP comprised of one share of Common Stock and three Common Stock purchase warrants with each unit priced at $4.00. Each warrant afforded the participant the opportunity to purchase the Company’s Common Stock at a warrant exercise price of $1.00. Each of the three warrants series has different expiration dates that have been extended.

The warrants became exercisable on May 2, 2016 and, in the case of ZNWAB continued to be exercisable through May 2, 2017 (1 year) and, in the case of ZNWAC continued to be exercisable through May 2, 2018 for ZNWAC (2 years) and May 2, 2019 for ZNWAD (3 years), respectively, at a per share exercise price of $1.00.

As of May 2, 2017, any outstanding ZNWAB warrants expired.

As of May 2, 2018, any outstanding ZNWAC warrants expired.

On November 1, 2016, the Company launched a unit offering (the “Unit Program”) under the Company’s DSPP pursuant to which participants could purchase units comprised of seven shares of Common Stock and seven Common Stock purchase warrants, at a per unit purchase price of $10.

The warrant has the symbol “ZNWAE.”

The ZNWAE warrants became exercisable on May 1, 2017 and continue to be exercisable through May 1, 2020 at a per share exercise price of $1.00. The warrant terms provide that if the Company’s Common Stock trades above $5.00 per share at the closing price for 15 consecutive trading days at any time prior to the expiration date of the warrant, the Company has the sole discretion to accelerate the termination the warrant upon providing 60 days advanced notice to the warrant holders.

On February 23, 2017, the Company filed a Form S-3 with the SEC (Registration No. 333-216191) as a replacement for the Form S-3 (Registration No. 333-193336), along with the base Prospectus and Supplemental Prospectus. The Form S-3, as amended, and the new base Prospectus became effective on March 10, 2017, along with the Prospectus Supplement that was filed and became effective on March 10, 2017. The Prospectus Supplement under Registration No. 333-216191 describes the terms of the DSPP and replaces the prior Prospectus Supplement, as amended, under the prior Registration No. 333-193336.

On May 22, 2017, the Company launched a new unit offering (the “New Unit Program”). The New Unit Program consisted of a new combination of common stock and warrants, a new time period in which to purchase under the program, and a new unit price, but otherwise the same unit program features, conditions and terms in the Prospectus Supplement applied. The New Unit Program terminated on July 12, 2017. This New Unit Program enabled participants to purchase Units of the Company’s securities where each Unit (priced at $250.00 each) was comprised of (i) the number of shares of Common Stock determined by dividing $250.00 (the price of one Unit) by the average of the high and low sale prices of the Company’s Common Stock as reported on the NASDAQ on the unit purchase date and (ii) Common Stock purchase warrants to purchase an additional 25 shares of Common Stock at a warrant exercise price of $1.00 per share.

The warrant has the symbol “ZNWAF.”

All ZNWAF warrants became exercisable on August 14, 2017 and continue to be exercisable through August 14, 2020 at a per share exercise price of $1.00. The warrant terms provide that if the Company’s Common Stock trades above $5.00 per share as the closing price for 15 consecutive trading days at any time prior to the expiration date of the warrant, the Company has the sole discretion to accelerate the termination date of the warrant upon providing 60 days advanced notice to the warrant holders.

On October 16, 2017, the Company initiated another Unit Option Program which terminated on December 6, 2017. This Unit Option Program enabled participants to purchase Units of the Company’s securities where each Unit (priced at $250.00 each) was comprised of (i) a certain number of shares of Common Stock determined by dividing $250.00 (the price of one Unit) by the average of the high and low sale prices of the Company’s Common Stock as reported on the NASDAQ on the unit purchase date and (ii) Common Stock purchase warrants to purchase an additional 15 shares of Common Stock at a warrant exercise price of $1.00 per share.

The warrant has the symbol “ZNWAG.”

The warrants became exercisable on January 8, 2018 and continue to be exercisable through January 8, 2021 at a per share exercise price of $1.00. The warrant terms provide that if the Company’s Common Stock trades above $5.00 per share as the closing price for 15 consecutive trading days at any time prior to the expiration date of the warrant, the Company has the sole discretion to accelerate the termination date of the warrant upon providing 60 days advanced notice to the warrant holders.

On February 1, 2018, the Company’s latest Unit Option began and terminated on February 28, 2018. The Unit Option consisted of Units of our securities where each Unit (priced at $250.00 each) was comprised of (i) 50 shares of Common Stock and (ii) Common Stock purchase warrants to purchase an additional 50 shares of Common Stock. The investor’s Plan account was credited with the number of shares of the Company’s Common Stock acquired under the Units purchased. Each warrant affords the investor the opportunity to purchase one share of Company Common Stock at a warrant exercise price of $5.00.

The warrant has the symbol “ZNWAH.”

The warrants became exercisable on April 2, 2018 and continue to be exercisable through April 2, 2019 at a per share exercise price of $5.00.

For the three months ended March 31, 2018, approximately $3,835,000 was raised under the DSPP program.

The warrants represented by the ticker ZNWAA are tradable on the NASDAQ market. However, all of the other warrants characterized above, in the table below, and throughout this Form 10-Q, are not tradeable and are used internally for classification and accounting purposes only.

The warrant transactions since January 1, 2018 are shown in the table below:

	ZNWAA	ZNWAC	ZNWAD	ZNWAE	ZNWAF	ZNWAG	ZNWAH	Total
Outstanding warrants,	1,524,617	275,152	294,334	3,028,119	460,231	414,300	-	5,996,753

December 31, 2017								
Exercise Price	$2.00	$1.00	$1.00	$1.00	$1.00	$1.00	$5.00	
Warrant Termination Date	1/31/2020	5/2/2018	5/2/2019	5/2/2020	8/14/2020	1/8/2021	4/2/2019	
Change during 2018 to:								
Issued	-	-	-	10,493	50	30	373,650	384,223
Exercised	(12,825)	(76,015)	(6,194)	(408,346)	(51,585)	(159,385)	-	(714,350)
Expired	-	-	-	-	-	-	-	-
Outstanding warrants, March 31, 2018	1,511,792	199,137	288,140	2,630,266	408,696	254,945	373,650	5,666,626

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Zion Oil & Gas, Inc.

Notes to Financial Statements

Note 3 - Stockholders' Equity (cont'd)

E. Warrant Descriptions

The price and the expiration dates for the series of warrants to investors are as follows:

	Period of Grant	US$	Expiration Date
ZNWAA Warrants	March 2013 – December 2014	2.00	January 31, 2020
ZNWAC Warrants	January 2015 – March 2016	1.00	May 02, 2018
ZNWAD Warrants	January 2015 – March 2016	1.00	May 02, 2019
ZNWAE Warrants	November 2016 – March 2017	1.00	May 01, 2020
ZNWAF Warrants	May 2017 – July 2017	1.00	August 14, 2020
ZNWAG Warrants	October 2017 – December 2017	1.00	January 08, 2021
ZNWAH Warrants	February 2018	5.00	April 2, 2019

Zion Oil & Gas, Inc.

Notes to Financial Statements

Note 4 - Unproved Oil and Gas Properties, Full Cost Method

Unproved oil and gas properties, under the full cost method, are comprised as follows:

	March 31, 2018 US$ thousands	December 31, 2017 US$ thousands
Excluded from amortization base:		
Drilling costs, and other operational related costs	18,465	14,999
Capitalized salary costs	2,371	2,034
Capitalized interest costs	432	346
Legal costs, license fees and other preparation costs	4,365	4,087
Other costs	301	229
	*25,934	21,695

*The unproved oil and gas properties balance at March 31, 2018 contains approximately $1,998,000 in unpaid amounts.

Changes in Unproved oil and gas properties during the three months ended March 31, 2018 and 2017 are as follows:

	March 31, 2018 US$ thousands	March 31, 2017 US$ thousands
Excluded from amortization base:		
Drilling costs, and other operational related costs	3,466	1,707
Capitalized salary costs	337	245
Capitalized interest costs	86	-
Legal costs, license fees and other preparation costs	278	103

Other costs	72	-
	*4,239	*2,055

* Inclusive of non-cash amounts of approximately $2,381,000 and $997,000 during the three months ended March 31, 2018, and 2017, respectively.

Note 5 - Senior Convertible Bonds

Rights Offering -10% Senior Convertible Notes due May 2, 2021

On October 21, 2015, the Company filed with the SEC a prospectus supplement for a rights offering. Under the rights offering, the Company distributed at no cost, 360,000 non-transferable subscription rights to subscribe for, on a per right basis, two 10% Convertible Senior Bonds par $100 due May 2, 2021 (the “Notes”), to persons who owned shares of the Company’s Common Stock on October 15, 2015, the record date for the offering. Each whole subscription right entitled the participant to purchase two convertible bonds at a purchase price of $100 per bond. Effective October 21, 2015, the Company executed a Supplemental Indenture, as issuer, with the American Stock Transfer & Trust Company, LLC, a New York limited liability trust company (“AST”), as trustee for the Notes (the “Indenture”).

On March 31, 2016, the rights offering terminated.

On May 2, 2016, the Company issued approximately $3,470,000 aggregate principal amount of Notes in connection with the rights offering. The Company received net proceeds of approximately $3,334,000, from the sale of the Notes, after deducting fees and expenses of $136,000 incurred in connection with the offering. These costs have been discounted as deferred offering costs.

The Notes contain a convertible option that gives rise to a derivative liability, which is accounted for separately from the Notes (see below and Note 6). Accordingly, the Notes were initially recognized at fair value of approximately $1,844,000, which represents the principal amount of $3,470,000 from which a debt discount of approximately $1,626,000 (which is equal to the fair value of the convertible option) was deducted.

During the three months ended March 31, 2018, the Company recorded approximately $6,000 in amortization expense related to the deferred financing costs, and approximately $80,000 in debt discount amortization. The Notes are governed by the terms of the Indenture. The Notes are senior unsecured obligations of the Company and bear interest at a rate of 10% per year, payable annually in arrears on May 2 of each year, commencing May 2, 2017. The Notes will mature on May 2, 2021, unless earlier redeemed by the Company or converted by the holder.

Interest and principal may be paid, at the Company’s option, in cash or in shares of the Company’s Common Stock. The number of shares for the payment of interest in shares of Common Stock, in lieu of the cash amount, will be based on the average of the closing prices of the Company’s Common Stock as reported by Bloomberg L.P. for the 30 trading days preceding the record date for the payment of interest; such record date has been designated and will always be the 10th business day prior to the interest payment date on May 2 of each year. The number of shares for the payment of principal, in lieu of the cash amount, shall be based upon the average of the closing price of the Company’s Common Stock as reported by Bloomberg L.P. for the 30 trading days preceding the principal repayment date; such record date has been designated as the trading day immediately prior to the 30-day period preceding the maturity date of May 2, 2021. Fractional shares will not be issued and the final number of shares will be rounded up to the next whole share.

On May 2, 2017, the Company paid its annual 10% interest to its bondholders of record on April 18, 2017. The interest was paid-in-kind (“PIK”) in the form of Common Stock. An average of the Company stock price of $1.20 was determined based on the 30 trading days prior to the record date of April 18, 2017. This figure was used to divide into 10% of the par value of the bonds held by the holders. The Company issued 289,213 shares to the accounts of its bondholders.

At any time prior to the close of business on the business day immediately preceding April 2, 2021, holders may convert their notes into Common Stock at the conversion rate of 44 shares per $100 bond (which is equivalent to a conversion rate of approximately $2.27 per share). The conversion rate is subject to adjustment from time to time upon the occurrence of certain events, including, but not limited to, the issuance of stock dividends and payment of cash dividends.

Beginning May 3, 2018, the Company is entitled to redeem for cash the outstanding Notes at an amount equal to the principal and accrued and unpaid interest, plus a 10% premium. No “sinking fund” is provided for the Notes due May 2021, which means that the Company is not required to periodically redeem or retire the Notes due May 2021.

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Zion Oil & Gas, Inc.

Notes to Financial Statements

Note 5 - Senior Convertible Bonds (cont'd)

Through the three months ended March 31, 2018 approximately 730 convertible bonds of $100 each, have been converted under this offering at a conversion rate of approximately $2.27 per share. As a result, the Company issued approximately 32,000 shares of its Common Stock during the same period.

	March 31, 2018 US$ thousands	December 31, 2017 US$ thousands
10% Senior Convertible Bonds, net of debt discount on derivative liability of $1,626,000 on the day of issuance	$ 1,844	$ 1,844
Debt discount amortization, net	$ 439	$ 359
Bonds converted to shares	$ (184)	$ (111)
Offering cost, net	$ (84)	$ (90)
10% senior Convertible bonds – Long Term Liability	$ 2,015	$ 2,002

The Company recognized $86,000 in capitalized interest for the three months ended March 31, 2018.

Note 6 - Derivative Liability

The Notes issued by the Company and discussed in Note 5 contain a convertible option that gives rise to a derivative liability.

The debt instrument the Company issued includes a make-whole provision, which provides that in the event of conversion by the investor under certain circumstances, the issuer is required to deliver to the holder additional consideration beyond the settlement of the conversion obligation.

Because time value make-whole provisions are not clearly and closely related to the debt host and would meet the definition of a derivative if considered freestanding, they should be evaluated under the indexation guidance to determine whether they would be afforded the scope exception pursuant to ASC 815-10-15-74(a). This evaluation is generally performed in conjunction with the analysis of the embedded conversion feature.

The Company has measured its derivative liability at fair value and recognized the derivative value as a current liability and recorded the derivative value on its balance sheet. The fair value of the shares to be issued upon conversion of the Notes was recorded as a derivative liability, with the change in the fair value recorded as a gain or loss in the accompanying statement of operations.

The valuation of the Notes was done by using the Binomial Model, a well-accepted option-pricing model, and based on the Notes' terms and other parameters the Company identified as relevant for the valuation of the Notes' Fair Value.

The Binomial Model used the forecast of the Company share price during the Note's contractual term.

Zion Oil & Gas, Inc.

Notes to Financial Statements

Note 6 - Derivative Liability (cont'd)

As of March 31, 2018, the Company's liabilities that are measured at fair value are as follows:

	March 31, 2018		December 31, 2017	
	Level 3	Total	Level 3	Total
	US$ thousands	US$ thousands	US$ thousands	US$ thousands
Fair value of derivative liability	5,400	5,400	1,866	1,866

Change in value of derivative liability during 2018 are as follows:

	US$ thousands
Derivative liability fair value at December 31, 2017	1,866
Loss on derivative liability	3,534
Derivative liability fair value at March 31, 2018	5,400

The following table presents the assumptions that were used for the model as of March 31, 2018:

	March 31, 2018	December 31, 2017
Convertible Option Fair Value of approximately	$5,400,000	$ 1,866,000
Annual Risk-free Rate	2.36 %	2.03 %

Volatility	79.03 %	68.04 %
Expected Term (years)	3.09	3.34
Convertible Notes Face Value	$3,285,900	$ 3,358,900
Expected annual yield on Regular Notes	28.77 %	28.77 %
Price of the Underlying Stock	$4.76	$ 2.16

During the three months ended March 31, 2018, the Company recorded a loss of approximately $3,534,000 (net) within the Statements of Operations line item, (loss) gain on derivative liability. A slight change in an unobservable input like volatility could have a significant impact on the fair value measurement of the derivative liability.

Note 7 - Commitments and Contingencies

A. Litigation

From time to time, the Company may be subject to routine litigation, claims, or disputes in the ordinary course of business. The Company defends itself vigorously in all such matters. In the opinion of management, no pending or known threatened claims, actions or proceedings against the Company are expected to have a material adverse effect on its financial position, results of operations or cash flows. However, the Company cannot predict with certainty the outcome or effect of any such litigation or investigatory matters or any other pending litigation or claims. There can be no assurance as to the ultimate outcome of any such lawsuits and investigations.

Zion Oil & Gas, Inc.

Notes to Financial Statements

Note 7 - Commitments and Contingencies (cont'd)

B. Environmental and Onshore Licensing Regulatory Matters

The Company is engaged in oil and gas exploration and production and may become subject to certain liabilities as they relate to environmental cleanup of well sites or other environmental restoration procedures and other obligations as they relate to the drilling of oil and gas wells or the operation thereof. Various guidelines have been published in Israel by the State of Israel's Petroleum Commissioner and Energy and Environmental Ministries as it pertains to oil and gas activities. Mention of these older guidelines was included in previous Zion Oil & Gas filings.

The Company acknowledges that these new regulations are likely increase both the time and the expenditures associated with obtaining new exploration rights and drilling new wells.

C. Bank Guarantees

As of March 31, 2018, the Company provided Israeli-required bank guarantees to various governmental bodies (approximately $1,356,000) and others (approximately $84,000) with respect to its drilling operation in an aggregate amount of approximately $1,440,000. The (cash) funds backing these guarantees and additional amounts added to support currency fluctuations as required by the bank are held in restricted interest-bearing accounts and are reported on the Company's balance sheets as fixed short-term bank deposits – restricted, and fixed long-term bank deposits – restricted.

Note 8 - Subsequent Events

(i)

On April 2, 2018 the Company announced an offering (“2018 Subscription Rights Offering”) through American Stock Transfer& Trust Company, LLC (the “Subscription Agent”), at no cost to the shareholders, of non-transferable Subscription Rights to purchase Rights (each “Right” and collectively, the “Rights”) of its securities to persons who owned shares of our Common Stock on April 13, 2018 (“the Record Date”). Pursuant to the 2018 Subscription Rights Offering, each holder of shares of common stock on the Record Date received non-transferable rights to subscribe for Rights, with each Right comprised of one share of our Common Stock, par value $0.01 per share (the "Common Stock") and one Common Stock Purchase Warrant to purchase an additional one share of Common Stock. Each Right may be purchased at a per Right subscription price of $5.00. Each Warrant affords the investor the opportunity to purchase one share of our Common Stock at a warrant exercise price of $3.00. The warrants will become exercisable on June 29, 2018 and will continue to be exercisable for one year thereafter.

Each shareholder received .10 (one tenth) of a subscription right (i.e. one subscription right for each 10 shares owned) for each share of the Company’s Common Stock owned on the Record Date. The 2018 Subscription Rights Offering terminates on May 31, 2018. In association with this 2018 Subscription Rights Offering, the Company incurred approximately $79,000 in agency and setup costs prior to March 31, 2018. These costs are properly classified on our balance sheet.

(ii) On April 6, 2018, options to purchase 14,000 shares of Common Stock were granted to seven staff members at an exercise price of $0.01 per share. The options vested upon grant and are exercisable through April 5, 2028. The fair value of the options at the date of grant amounted to approximately $62,000.

(iii) Approximately $1,000,000 was raised through the Company’s DSPP program from April 1 through 26, 2018.

(iv) On May 2, 2018, the Company paid its annual 10% interest to its bondholders of record on April 18, 2018. The interest was paid-in-kind (“PIK”) in the form of Common Stock. An average Zion stock price of $4.679 was determined based on the 30 trading days prior to the record date of April 18, 2018. This figure was used to divide into 10% of the par value of the bonds held by the holders. The company issued 70,780 shares to the accounts of its bondholders.

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

THE FOLLOWING DISCUSSION SHOULD BE READ IN CONJUNCTION WITH OUR UNAUDITED INTERIM FINANCIAL STATEMENTS AND THE RELATED NOTES TO THOSE STATEMENTS INCLUDED IN THIS FORM 10-Q. SOME OF OUR DISCUSSION IS FORWARD-LOOKING AND INVOLVES RISKS AND UNCERTAINTIES. FOR INFORMATION REGARDING RISK FACTORS THAT COULD HAVE A MATERIAL ADVERSE EFFECT ON OUR BUSINESS, REFER TO THE DISCUSSION OF RISK FACTORS IN THE "DESCRIPTION OF BUSINESS" SECTION OF OUR ANNUAL REPORT ON FORM 10-K FOR THE YEAR ENDED DECEMBER 31, 2017, FILED WITH THE SECURITIES AND EXCHANGE COMMISSION.

Forward-Looking Statements

Certain statements made in this discussion are "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. These statements may materially differ from actual results.

Forward-looking statements can be identified by terminology such as "may", "should", "expects", "intends", "anticipates", "believes", "estimates", "predicts", or "continue" or the negative of these terms or other comparable terminology and include, without limitation, statements regarding:

Our ability to raise sufficient capital to successfully test, complete and produce our current exploratory well if applicable and continue with exploratory efforts within our license area;

the going concern qualification in our financial statements;

our ability to explore for and develop oil and natural gas resources successfully and economically;

our liquidity and our ability to raise capital to finance our exploration and development activities;

our ability to maintain the exploration license rights to continue our petroleum exploration program;

the availability of equipment, such as seismic equipment, drilling rigs, and production equipment;

the impact of governmental regulations, permitting and other legal requirements in Israel relating to onshore exploratory drilling;

our estimates of the time frame within which the drilling of our exploratory well and the exploratory activities will be undertaken;

changes in our drilling plans and related budgets;

the quality of existing and future license areas with regard to, among other things, the existence of reserves in economic quantities;

anticipated trends in our business;

our future results of operations;

our capital expenditure program;

future market conditions in the oil and gas industry; and

the demand for oil and natural gas, both locally in Israel and globally.

Overview

Zion Oil and Gas, Inc., a Delaware corporation, is an oil and gas exploration company with a history of over 18 years of oil and gas exploration in Israel. We were incorporated in Florida on April 6, 2000 and reincorporated in Delaware on July 9, 2003. We completed our initial public offering in January 2007. Our common stock, par value $0.01 per share (the “Common Stock”), currently trades on the NASDAQ Global Market under the symbol “ZN” and our Common Stock warrant under the symbol “ZNWAA.”

The Company currently holds one active petroleum exploration license onshore Israel, the Megiddo-Jezreel License, comprising approximately 99,000 acres. The Megiddo Jezreel #1 (“MJ #1”) site was completed in early March 2017, after which the drilling rig and associated equipment were mobilized to the site. Performance and endurance tests were completed, and the MJ #1 exploratory well was spud on June 5, 2017, ahead of the June 30, 2017 deadline under the then-existing license terms. The MJ #1 well has been drilled to a total depth (“TD”) of 5,060 meters (approximately 16,600 feet). Thereafter, the Company obtained three open-hole wireline log suites (including a formation image log) and the well was successfully cased and cemented in preparation for upcoming testing of multiple zones of interest, including zone(s) where free-flowing hydrocarbons were collected after circulating mud in the borehole. After our review of the open-hole logs, we have finalized the testing program. The Ministry of Energy approved the well testing protocol on April 29, 2018. We have begun our testing program, and it may take several weeks to complete.

Zion has encountered movable oil and gas in the well’s drilling mud. However, as of the date of this report on Form 10-Q, we are not able to confirm whether the well will be commercially productive and will not be able to do so until after testing and evaluation of the MJ#1 well is complete.

Depending on the results of the MJ #1 exploratory well and having adequate cash resources, multiple wells could be drilled from this pad site, as several subsurface geologic targets are reachable using directional well trajectories.

At present, we have no revenues or operating income. Our ability to generate future revenues and operating cash flow will depend on the successful exploration and exploitation of our current and any future petroleum rights or the acquisition of oil and/or gas producing properties, and the volume and timing of such production. In addition, even if we are successful in producing oil and gas in commercial quantities, our results will depend upon commodity prices for oil and gas, as well as operating expenses including taxes and royalties.

Our executive offices are located at 12655 North Central Expressway, Suite 1000, Dallas, Texas 75243, and our telephone number is (214) 221-4610. Our branch office’s address in Israel is 9 Halamish Street, North Industrial Park, Caesarea 3088900, and the telephone number is +972-4-623-8500. Our website address is: www.zionoil.com.

Current Exploration and Operation Efforts

Megiddo-Jezreel Petroleum License

Zion currently holds one active petroleum exploration license onshore Israel, the Megiddo-Jezreel License (covering an area of approximately 99,000 acres – See Map 1). Under Israeli law, Zion has an exclusive right to oil and gas exploration in our license area in that no other company may drill there. In the event we drill an oil or gas discovery in our license area, current Israeli law entitles us to convert the relevant portions of our license to a 30-year production lease, extendable to 50 years, subject to compliance with a field development work program and production.

Map 1. Zion's Megiddo-Jezreel Petroleum Exploration License as of May, 2018.

The Megiddo-Jezreel License was awarded on December 3, 2013 for a three-year primary term through December 2, 2016, with the possibility of additional one-year extensions up to a maximum of seven years. The MJL (~99,000 acres) is onshore, south and west of the Sea of Galilee. In November of 2016, the State of Israel's Petroleum Commissioner officially approved the Company's drilling date and license extension request.

On October 30, 2017, Zion sought a multi-year extension to its existing license. After receiving feedback from Israel's Petroleum Commissioner, Zion submitted a revised extension request on November 9, 2017. On November 20, 2017, Israel's Petroleum Commissioner officially approved Zion's multi-year extension request on its Megiddo-Jezreel License No. 401, extending its validity to December 2, 2019. The Company now remains subject to the following updated key license terms:

Number	***Activity Description***	***Execution by:***
1	*Submit final report on the results of drilling*	*31 May 2018*
2	*Submit program for continuation of work under license*	*30 June 2018*

Although the Company's MJ #1 well has reached its total depth and is currently undergoing formation testing, as of the date of this report on Form 10-Q, we are not able to confirm whether the well will be commercially productive and will not be able to do so until after fully testing and evaluating the well.

Depending on the final outcome and results of the currently active MJ #1 well and having adequate cash resources, multiple wells could be drilled from this pad site as several subsurface geologic targets are reachable using directional well trajectories.

We continue our exploration focus on our Megiddo-Jezreel License area as that area appears to possess the key geologic ingredients of an active petroleum system.

Zion's Former Asher-Menashe and Joseph Licenses

Zion has plugged all of its exploratory wells on its former Asher-Menashe and Joseph License areas, and the reserve pits have been evacuated, but acknowledges its obligation to complete the abandonment of these well sites in accordance with guidance from the Energy Ministry, Environmental Ministry and local officials.

Onshore Licensing, Oil and Gas Exploration and Environmental Guidelines

The Company is engaged in oil and gas exploration and production and may become subject to certain liabilities as they relate to environmental cleanup of well sites or other environmental restoration procedures and other obligations as they relate to the drilling of oil and gas wells or the operation thereof. Various guidelines have been published in

Israel by the State of Israel's Petroleum Commissioner, the Energy Ministry, and the Environmental Ministry since 2012 as it pertains to oil and gas activities. Mention of these guidelines was included in previous Zion Oil & Gas filings.

We acknowledge that these new regulations are likely to increase the expenditures associated with obtaining new exploration rights and drilling new wells. The company expects that additional financial burdens could occur as a result of the Ministry requiring cash reserves that could otherwise be used for operational purposes.

Capital Resources Highlights

We need to raise significant funds to finance the continued exploration and production efforts and maintain orderly operations. To date, we have funded our operations through the issuance of our securities and convertible debt. We will need to continue to raise funds through the issuance of equity and/or debt securities (or securities convertible into or exchangeable for equity securities). No assurance can be provided that we will be successful in raising the needed equity on terms favorable to us (or at all).

The Dividend Reinvestment and Stock Purchase Plan

On March 27, 2014, the Company launched its Dividend Reinvestment and Stock Purchase Plan (the "DSPP") pursuant to which stockholders and interested investors could purchase shares of the Company's Common Stock as well as units of the Company's securities. The terms of the DSPP are described in the Prospectus Supplement originally filed on March 31, 2014 (the "Original Prospectus Supplement") with the Securities and Exchange Commission ("SEC") under the Company's effective registration Statement on Form S-3, as thereafter amended.

On February 23, 2017, the Company filed a Form S-3 with the SEC (Registration No. 333-216191) as a replacement for the Form S-3 (Registration No. 333-193336), in which the three (3) year period was ending March 31, 2017, along with the base Prospectus and Supplemental Prospectus. The Form S-3, as amended, and the new base Prospectus became effective on March 10, 2017, along with the Prospectus Supplement that was filed and became effective on March 10, 2017. The Prospectus Supplement under Registration No. 333-216191 describes the terms of the DSPP and replaces the prior Prospectus Supplement, as amended, under the prior Registration No. 333-193336.

Please see Footnote 3E ("Dividend Reinvestment and Stock Purchase Plan ("DSPP")), which is a part of this Form 10-Q filing, for details about specific unit programs, dates, and filings during the years 2015 through 2017.

For the three months ended March 31, 2018, approximately $3,835,000 was raised under the DSPP program. Of this amount, approximately $727,000 was received through the exercise of warrants, representing 19% of the $3,835,000 total received.

The Warrants transactions since January 1, 2018 are shown in the table below:

	ZNWAA	ZNWAC	ZNWAD	ZNWAE	ZNWAF	ZNWAG	ZNWAH	Total
Outstanding warrants, December 31, 2017	1,524,617	275,152	294,334	3,028,119	460,231	414,300	-	5,996,753
Exercise Price	$2.00	$1.00	$1.00	$1.00	$1.00	$1.00	$5.00	
Warrant Termination Date	1/31/2020	5/2/2018	5/2/2019	5/2/2020	8/14/2020	1/8/2021	4/2/2019	
Change during 2018 to:								
Issued	-	-	-	10,493	50	30	373,650	384,223
Exercised	(12,825)	(76,015)	(6,194)	(408,346)	(51,585)	(159,385)	-	(714,350)
Expired	-	-	-	-	-	-	-	-
Outstanding warrants, March 31, 2018	1,511,792	199,137	288,140	2,630,266	408,696	254,945	373,650	5,666,626

According to the warrant table, the Company could potentially raise up to approximately $8,673,000 if all outstanding warrants were exercised by its holders.

10% Senior Convertible Notes due May 2, 2021

On October 21, 2015, the Company filed with the SEC a prospectus supplement for a rights offering. Under the rights offering, the Company distributed at no cost, 360,000 non-transferable subscription rights to subscribe for, on a per right basis, two 10% Convertible Senior Bonds par $100 due May 2, 2021 (the “Notes”), to persons who owned shares of the Company’s Common Stock on October 15, 2015, the record date for the offering. Each whole subscription right entitled the participant to purchase two convertible bonds at a purchase price of $100 per bond. Effective October 21, 2015, the Company executed a Supplemental Indenture, as issuer, with the American Stock Transfer & Trust Company, LLC, a New York limited liability trust company (“AST”), as trustee for the Notes (the “Indenture”).

The offering was scheduled to terminate on January 15, 2016 but was extended to March 31, 2016. On March 31, 2016, the rights offering terminated.

On May 2, 2016, the Company issued approximately $3,470,000 aggregate principal amount of Notes in connection with the rights offering. The Company received net proceeds of approximately $3,334,000 from the sale of the Notes after deducting fees and expenses of $136,000 incurred in connection with the offering. These costs have been discounted as deferred offering costs.

The Notes contain a convertible option that gives rise to a derivative liability, which is accounted for separately from the Notes (see below and Note 8). Accordingly, the Notes were initially recognized at fair value of approximately $1,844,000, which represents the principal amount of $3,470,000 from which a debt discount of approximately $1,626,000 (which is equal to the fair value of the convertible option) was deducted.

During the three months ended March 31, 2018, the Company recorded approximately $28,000 in amortization expense related to the deferred financing costs, and approximately $80,000 in debt discount amortization, net. The Notes are governed by the terms of the Indenture. The Notes are senior unsecured obligations of the Company and bear interest at a rate of 10% per year, payable annually in arrears on May 2 of each year, commencing May 2, 2017. The Notes will mature on May 2, 2021, unless earlier redeemed by the Company or converted by the holder.

Interest and principal may be paid, at the Company’s option, in cash or in shares of the Company’s Common Stock. The number of shares for the payment of interest in shares of Common Stock, in lieu of the cash amount, will be based on the average of the closing prices of the Company’s Common Stock as reported by Bloomberg L.P. for the 30 trading days preceding the record date for the payment of interest; such record date has been designated and will always be the 10th business day prior to the interest payment date on May 2 of each year. The number of shares for the payment of principal, in lieu of the cash amount, shall be based upon the average of the closing price of the Company’s

Common Stock as reported by Bloomberg L.P. for the 30 trading days preceding the principal repayment date; such record date has been designated as the trading day immediately prior to the 30-day period preceding the maturity date of May 2, 2021. Fractional shares will not be issued, and the final number of shares will be rounded up to the next whole share.

On May 2, 2017, the Company paid its annual 10% interest to its bondholders of record on April 18, 2017. The interest was paid-in-kind ("PIK") in the form of Common Stock. An average Zion stock price of $1.196 was determined based on the 30 trading days prior to the record date of April 18, 2017. This figure was used to divide into 10% of the par value of the bonds held by the holders. The Company issued 289,213 shares to the accounts of its bondholders.

At any time prior to the close of business on the business day immediately preceding April 2, 2021, holders may convert their notes into Common Stock at the conversion rate of 44 shares per $100 bond (which is equivalent to a conversion rate of approximately $2.27 per share). The conversion rate is subject to adjustment from time to time upon the occurrence of certain events, including, but not limited to, the issuance of stock dividends and payment of cash dividends.

Beginning May 3, 2018, the Company is entitled to redeem for cash the outstanding Notes at an amount equal to the principal and accrued and unpaid interest, plus a 10% premium. No “sinking fund” is provided for the Notes, which means that the Company is not required to periodically redeem or retire the Notes due May 2021.

Through the three months ended March 31, 2018 approximately 730 convertible bonds of $100 each, have been converted under this offering at a conversion rate of approximately $2.27 per share. As a result, the Company issued approximately 32,000 shares of its Common Stock during the same period.

The Company recognized $86,000 in capitalized interest for the three months ended March 31, 2018. The Company recognized $ 0 as interest expense for the three months ended March 31, 2018. On May 2, 2017, the Company paid its annual 10% interest (in-kind) to the bondholders of record on April 18, 2017.

2018 Subscription Rights Offering

On April 2, 2018 the Company announced an offering (“2018 Subscription Rights Offering”) through American Stock Transfer& Trust Company, LLC (the “Subscription Agent”), at no cost to the shareholders, non-transferable Subscription Rights to purchase Rights (each “Right” and collectively, the “Rights”) of its securities to persons who owned shares of our Common Stock on April 13, 2018 (“the Record Date”). Pursuant to the 2018 Subscription Rights Offering, each holder of shares of common stock on the Record Date received non-transferable rights to subscribe for Rights, with each Right comprised of one share of our Common Stock, par value $0.01 per share (the "Common Stock") and one Common Stock Purchase Warrant to purchase an additional one share of Common Stock. Each Right may be purchased at a per Right subscription price of $5.00. Each Warrant affords the investor the opportunity to purchase one share of our Common Stock at a warrant exercise price of $3.00. The warrants will become exercisable on June 29, 2018 and will continue to be exercisable for one year thereafter.

Each shareholder received .10 (one tenth) of a subscription right (i.e. one subscription right for each 10 shares owned) for each share of the Company’s Common Stock owned on the Record Date. The 2018 Subscription Rights Offering terminates on May 31, 2018.

A total of 5,720,000 Rights have been set aside by the Company for this 2018 Subscription Rights Offering. At $5.00 for each Right, the Company could potentially raise up to $28,600,000 (exclusive of an estimated $250,000 in offering costs) if all rights were subscribed by shareholders. At a $3.00 exercise price for the warrants, an additional $17,160,000 could potentially be raised from the warrants, beginning on June 29, 2018, provided that all warrants will be exercised. No assurance can be given that these figures will be reached, or even close to it.

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Principal Components of our Cost Structure

Our operating and other expenses primarily consist of the following:

Impairment of Unproved Oil and Gas Properties: Impairment expense is recognized if a determination is made that a well will not be able to be commercially productive. The amounts include amounts paid in respect of the drilling operations as well as geological and geophysical costs and various amounts that were paid to Israeli regulatory authorities.

General and Administrative Expenses: Overhead, including payroll and benefits for our corporate staff, costs of managing our exploratory operations, audit and other professional fees, and legal compliance is included in general and administrative expenses. General and administrative expenses also include non-cash stock-based compensation expense, investor relations related expenses, lease and insurance and related expenses.

Depreciation, Depletion, Amortization and Accretion: The systematic expensing of the capital costs incurred to explore for natural gas and oil represents a principal component of our cost structure. As a full cost company, we capitalize all costs associated with our exploration, and apportion these costs to each unit of production, if any, through depreciation, depletion and amortization expense. As we have yet to have production, the costs of abandoned wells are written off immediately versus being included in this amortization pool.

Going Concern Basis

Since we have limited capital resources, no revenue to date and a loss from operations, our financial statements have been prepared on a going concern basis, which contemplates realization of assets and liquidation of liabilities in the ordinary course of business. The appropriateness of using the going concern basis is dependent upon our ability to obtain additional financing or equity capital and, ultimately, to achieve profitable operations. Therefore, there is substantial doubt about our ability to continue as a going concern. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

Critical Accounting Policies

Management’s discussion and analysis of financial condition and results of operations is based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expense during the reporting period.

Impairment of Oil and Gas Properties

We follow the full-cost method of accounting for oil and gas properties. Accordingly, all costs associated with acquisition, exploration and development of oil and gas reserves, including directly related overhead costs, are capitalized.

All capitalized costs of oil and gas properties, including the estimated future costs to develop proved reserves, are amortized on the unit-of-production method using estimates of proved reserves. Investments in unproved properties and major development projects are not amortized until proved reserves associated with the projects can be determined or until impairment occurs. If the results of an assessment indicate that the properties are impaired, the amount of the impairment is included in income from continuing operations before income taxes, and the adjusted carrying amount of the unproved properties is amortized on the unit-of-production method.

Our oil and gas properties represent an investment in unproved properties. These costs are excluded from the amortized cost pool until proved reserves are found or until it is determined that the costs are impaired. All costs excluded are reviewed at least quarterly to determine if impairment has occurred. The amount of any impairment is charged to expense since a reserve base has not yet been established. A further impairment requiring a charge to expense may be indicated through evaluation of drilling results, relinquishing drilling rights or other information.

Abandonment of properties is accounted for as adjustments to capitalized costs. The net capitalized costs are subject to a "ceiling test" which limits such costs to the aggregate of the estimated present value of future net revenues from proved reserves discounted at ten percent based on current economic and operating conditions, plus the lower of cost or fair market value of unproved properties. The recoverability of amounts capitalized for oil and gas properties is dependent upon the identification of economically recoverable reserves, together with obtaining the necessary financing to exploit such reserves and the achievement of profitable operations.

During the three months end March 31, 2018, and 2017, the Company did not record any non-cash impairment.

The total net book value of our unproved oil and gas properties under the full cost method was $25,934,000 at March 31, 2018.

Asset Retirement Obligation

We record a liability for asset retirement obligation at fair value in the period in which it is incurred and a corresponding increase in the carrying amount of the related long lived assets.

Fair Value Considerations

We follow ASC 820, “Fair Value Measurements and Disclosures,” as amended by Financial Accounting Standards Board (FASB) Financial Staff Position (FSP) No. 157 and related guidance. Those provisions relate to the Company’s financial assets and liabilities carried at fair value and the fair value disclosures related to financial assets and liabilities. ASC 820 defines fair value, expands related disclosure requirements, and specifies a hierarchy of valuation techniques based on the nature of the inputs used to develop the fair value measures. Fair value is defined as the price that would be received from the sale of an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, assuming the transaction occurs in the principal or most advantageous market for that asset or liability.

There are three levels of inputs to fair value measurements - Level 1, meaning the use of quoted prices for identical instruments in active markets; Level 2, meaning the use of quoted prices for similar instruments in active markets or quoted prices for identical or similar instruments in markets that are not active or are directly or indirectly observable; and Level 3, meaning the use of unobservable inputs. We use Level 1 inputs for fair value measurements whenever there is an active market, with actual quotes, market prices, and observable inputs on the measurement date. We use Level 2 inputs for fair value measurements whenever there are quoted prices for similar securities in an active market or quoted prices for identical securities in an inactive market. We use observable market data whenever available. We use Level 3 inputs in the Binomial Model used for the valuation of the derivative liability.

Derivative Liabilities

In accordance with ASC 815-40-25 and ASC 815-10-15 Derivatives and Hedging and ASC 480-10-25 Liabilities-Distinguishing Liabilities from Equity, the embedded derivatives associated with the Convertible Bonds are accounted for as liabilities during the term of the related Convertible Bonds.

RESULTS OF OPERATIONS

	For the three months ended March 31	
	2018	2017
	(US $ in thousands)	
Operating costs and expenses:		
General and administrative expenses	1,959	2,847
Other	553	676
Subtotal Operating costs and expenses	2,512	3,523
Loss (gain) on derivative liability	3,534	(273)
Other expense, net	205	125
Net loss	6,251	3,375

Revenue. We currently have no revenue generating operations.

Operating costs and expenses. Operating costs and expenses for the three months ended March 31, 2018 were $2,512,000 compared to $3,523,000 for the three months ended March 31, 2017. The decrease in operating costs and expenses during the three months ended March 31, 2018 compared to the corresponding period in 2017 is primarily attributable to decrease in general and administrative expenses driven by the non-cash expenses associated with stock option grants, and by a decrease in other expenses.

General and administrative expenses. General and administrative expenses for the three months ended March 31, 2018 were $1,959,000, compared to $2,847,000 for the three months ended March 31, 2017. The decrease in general and administrative expenses during the three months ended March 31, 2018 compared to the corresponding period in 2017 is primarily attributable to lower non-cash expenses recorded in connection with stock option grants during 2018.

Other expenses. Other expenses during the three months ended March 31, 2018 were $553,000, compared to $676,000 for the three months ended March 31, 2017. Other general and administrative expenses are comprised of non-compensation and non-professional expenses incurred. The decrease in other general and administrative expenses during the three months ended March 31, 2018 compared to the corresponding period in 2017 is primarily attributable to less marketing expenses associated with investor relations activities.

Loss, (gain) on derivative liability. Loss, (gain) on derivative liability during the three months ended March 31, 2018 was $3,534,000 compared to ($273,000) for the three months ended March 31, 2017. An embedded derivative is contained within the valuation of Zion's $100 convertible bond offering which closed in March 2016. The loss on derivative liability during the three months ended March 31, 2018 compared to the gain on derivative liability during the three months ended March 31, 2017 is primarily due to the increase in the share price of our common stock that occurred during the three months ended March 31, 2018.

Other expense, net. Other expense, net for the three months ended March 31, 2018 was $205,000 compared to $125,000 for the three months ended March 31, 2017. The increase in other expense, net during the three months ended March 31, 2018 compared to the corresponding period in 2017 is primarily attributable to exchange rate differences associated with the fluctuating exchange rates of the New Israeli Shekels ("NIS") with the U.S. Dollar ("USD").

Net Loss. Net loss for the three months ended March 31, 2018 was $6,251,000 compared to $3,375,000 for the three months ended March 31, 2017.

Liquidity and Capital Resources

Liquidity is a measure of a company's ability to meet potential cash requirements. As discussed above, we have historically met our capital requirements through the issuance of our securities as well as proceeds from the issuance of convertible debt, as well as proceeds from the exercise of warrants and options to purchase common equity.

Our ability to continue as a going concern is dependent upon obtaining the necessary financing to complete further exploration and development activities and generate profitable operations from our oil and natural gas interests in the future. Our current operations are dependent upon the adequacy of our current assets to meet our current expenditure requirements and the accuracy of management's estimates of those requirements. Should those estimates be materially incorrect, our ability to continue as a going concern will be impaired. Our unaudited interim financial statements for the three months ended March 31, 2018 have been prepared on a going concern basis, which contemplates the realization of assets and the settlement of liabilities and commitments in the normal course of business. We have incurred a history of operating losses and negative cash flows from operations. Therefore, there is substantial doubt about our ability to continue as a going concern.

At March 31, 2018, we had approximately $4,770,000 in cash and cash equivalents compared to $6,892,000 at December 31, 2017, which does not include any restricted funds. Our working capital (current assets minus current liabilities) was $(1,602,000) at March 31, 2018 and $3,646,000 at December 31, 2017. The derivative liability at March 31, 2018 was $5,400,000 and this non-cash liability negatively impacts the working capital figure. Our working capital balances, exclusive of the non-cash derivative liability amounts, were $3,798,000 at March 31, 2018 and $5,512,000 at December 31, 2017.

As of March 31, 2018, we provided bank guarantees to various governmental bodies (approximately $1,356,000) and others (approximately $84,000) in respect of our drilling operation in the aggregate amount of approximately $1,440,000. The (cash) funds backing these guarantees and additional amounts added to support currency fluctuations as required by the bank are held in restricted interest-bearing accounts and are reported on the Company's balance sheets as fixed short-term bank deposits – restricted, and fixed long-term bank deposits – restricted.

During the three months ended March 31, 2018, cash used in operating activities totaled $985,000. Cash provided by financing activities during the three months ended March 31, 2018 was $3,754,000 and is primarily attributable to proceeds received from the DSPP. Net cash used in investing activities, such as unproved oil and gas properties, other assets and restricted bank deposits was $4,891,000 for the three months ended March 31, 2018.

We expect to incur additional significant expenditures to further our exploration and development programs. We estimate that, when we are not actively drilling a well, our expenditures are approximately $500,000 per month excluding exploratory operational activities. However, when we are actively drilling, testing or completing a well, we estimate an additional minimum expenditure of approximately $2,500,000 per month. The above estimates are subject to change. Management believes that our existing cash balance, coupled with anticipated proceeds under the DSPP, will be sufficient to finance our plan of operations, through July 31, 2018.

We will need to raise funds in order to drill our next exploratory well to the desired depth and to conduct any post drilling testing that may be required. No assurance can be provided that we will be able to raise the needed operating capital through our current rights offering that is continuing through May 31, 2018.

Even if we raise the needed funds from the current rights offering, there are factors that can nevertheless adversely impact our ability to fund our operating needs, including (without limitation), unexpected or unforeseen cost overruns in planned non-drilling exploratory work (e.g., drilling and environmental permit acquisition costs, etc.) in existing license areas and the costs associated with extended delays in undertaking the required exploratory work, which is typical of what we have experienced in the past, or plugging and abandonment activities.

Reference is made to the discussion above under **Capital Resources Highlights** for information relating to working capital that we raised through March 31, 2018.

Off-Balance Sheet Arrangements

We do not currently use any off-balance sheet arrangements to enhance our liquidity or capital resource position, or for any other purpose.

Recently Issued Accounting Pronouncements

The Company does not believe that the adoption of any recently issued accounting pronouncements in 2018 had a significant impact on our financial position, results of operations, or cash flow.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risk is a broad term for the risk of economic loss due to adverse changes in the fair value of a financial instrument. These changes may be the result of various factors, including interest rates, foreign exchange rates, commodity prices and/or equity prices. In the normal course of doing business, we are exposed to the risks associated with foreign currency exchange rates and changes in interest rates.

Foreign Currency Exchange Rate Risks. A portion of our expenses, primarily labor expenses and certain supplier contracts, are denominated in New Israeli Shekels ("NIS"). As a result, we have significant exposure to the risk of fluctuating exchange rates with the U.S. Dollar ("USD"), our primary reporting currency. During the period January 1, 2018 through March 31, 2018, the USD has fluctuated by approximately 1.4% against the NIS. During the period January 1, 2017 through December 31, 2017, the USD fluctuated by approximately (9.8%) against the NIS. Continuing devaluation of the US dollar against the NIS will result in higher operating costs from NIS denominated expenses. To date, we have not hedged any of our currency exchange rate risks, but we may do so in the future.

Interest Rate Risk. Our exposure to market risk relates to our cash and investments. We maintain an investment portfolio of short term bank deposits and money market funds. The securities in our investment portfolio are not leveraged, and are, due to their very short-term nature, subject to minimal interest rate risk. We currently do not hedge interest rate exposure. Because of the short-term maturities of our investments, we do not believe that a change in market interest rates would have a significant negative impact on the value of our investment portfolio except for reduced income in a low interest rate environment. At March 31, 2018, we had cash, cash equivalents and short-term bank deposits, inclusive of restricted cash, of approximately $5,354,000. The weighted average annual interest rate related to our cash and cash equivalents for the three months ended March 31, 2018 was approximately 0.10%.

The primary objective of our investment activities is to preserve principal while at the same time maximizing yields without significantly increasing risk. To achieve this objective, we invest our excess cash in short-term bank deposits and money market funds that may invest in high quality debt instruments.

ITEM 4. CONTROLS AND PROCEDURES

We maintain disclosure controls and procedures designed to ensure that information required to be disclosed in the reports that we file or submit under the Securities Exchange Act of 1934, is recorded, processed, summarized and reported within the time period specified in the SEC's rules and forms. As of March 31, 2018, our chief executive officer and our chief financial officer conducted an evaluation of the effectiveness of our disclosure controls and procedures. Based on this evaluation, our chief executive officer and our chief financial officer concluded that our disclosure controls and procedures were effective as of March 31, 2018.

Changes in Internal Control over Financial Reporting

During the quarter ended March 31, 2018, there were no changes made in our internal controls over financial reporting (as such term is defined in Rule 13a-15(f) of the Exchange Act) that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II—OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

From time to time, we may be subject to routine litigation, claims, or disputes in the ordinary course of business. We defend our company vigorously in all such matters. However, we cannot predict with certainty the outcome or effect of any of the litigation or investigatory matters or any other pending litigation or claims. There can be no assurance as to the ultimate outcome of these lawsuits and investigations.

ITEM 1A. RISK FACTORS

During the quarter ended March 31, 2018, there were no material changes to the risk factors previously reported in our Annual Report on Form 10-K for the year ended December 31, 2017.

ITEM 2. UNREGISTERED SALES OF SECURITIES AND USE OF PROCEEDS

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

None.

ITEM 5. OTHER INFORMATION:

None.

ITEM 6. EXHIBITS

Exhibit Index:

31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 under the Exchange Act
31.2	Certification of the Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 under the Exchange Act
32.1	Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (furnished only)
32.2	Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (furnished only)
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema
101.CAL	XBRL Taxonomy Extension Calculation Linkbase
101.DEF	XBRL Taxonomy Extension Definition Linkbase
101.LAB	XBRL Taxonomy Extension Label Linkbase
101.PRE	XBRL Taxonomy Extension Presentation Linkbase

SIGNATURES

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

ZION OIL & GAS, INC.
(Registrant)

By:	/s/ Victor G. Carrillo	By:	/s/ Michael B. Croswell Jr.
	Victor G. Carrillo		Michael B. Croswell Jr.
	Chief Executive Officer		Chief Financial Officer
	(Principal Executive Officer)		(Principal Financial and Accounting Officer)
Date:	May 8, 2018	Date:	May 8, 2018