GEOPETRO RESOURCES CO
Form 10-Q
November 09, 2009
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2009

OR

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

For the transition period from to

Commission file number 001-16749

GeoPetro Resources Company

(Exact name of registrant as specified in its charter)

California	**94-3214487**
(State of incorporation)	(IRS Employer Identification Number)
One Maritime Plaza, Suite 700 **San Francisco, CA**	**94111**
(Address of principal executive offices)	(Zip Code)

(415) 398-8186

(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 x No o.

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 o No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of large accelerated filer, accelerated filer, and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

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

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

There were 34,284,646 shares of no par value common stock outstanding on November 9, 2009.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements.

GEOPETRO RESOURCES COMPANY

UNAUDITED CONSOLIDATED BALANCE SHEETS

	September 30, 2009	December 31, 2008
ASSETS		
Current assets:		
Cash and cash equivalents	$ 1,645,006	$ 770,779
Trade accounts receivable natural gas sales	278,864	4,266
Accounts receivable other	22,836	35,107
Prepaid expenses	133,855	212,938
Total current assets	2,080,561	1,023,090
Oil and gas properties, at cost (full cost method):		
Unproved properties	9,953,679	10,500,498
Proved properties	49,572,988	48,346,939
Gas processing plant, at cost	10,285,573	10,707,982
Less accumulated depletion, depreciation, and impairment	(18,611,636)	(16,522,304)
Net oil and gas properties	51,200,604	53,033,115
Furniture, fixtures and equipment, at cost, net of depreciation	2,942	12,364
Other assets deposits and other noncurrent assets	16,127	7,436
Total Assets	$ 53,300,234	$ 54,076,005
LIABILITIES AND SHAREHOLDERS EQUITY		
Current Liabilities:		
Trade payables	$ 1,926,008	$ 1,137,432
Current portion of long term notes payable	1,254,582	600,000
Interest payable	114,851	1,479
Dividends payable	68,583	
Production taxes payable	331,525	311,168
Other taxes payable		20,833
Royalty owners payable	1,101,401	1,103,830
Total current liabilities	4,796,950	3,174,742
Long Term Notes Payable	5,830,507	7,019,449
Asset Retirement Obligations	63,478	59,099
Total Liabilities	10,690,935	10,253,290
Commitments and Contingencies (Notes 2 and 8)		

Shareholders Equity:				
Series B preferred stock, no par value; 6,800,000 shares authorized 4,121,004 shares issued and outstanding at September 30, 2009. Liquidation preference of $3,159,246 at September 30, 2009.		3,031,710		
Common stock, no par value; 100,000,000 shares authorized; 34,284,646 shares issued and outstanding at September 30, 2009 and December 31, 2008, respectively		53,397,733		53,397,733
Additional paid-in capital		2,936,739		2,610,596
Accumulated deficit		(16,756,883)		(12,185,614)
Total shareholders equity		42,609,299		43,822,715
Total Liabilities and Shareholders Equity	$	53,300,234	$	54,076,005

See accompanying notes to these unaudited consolidated financial statements.

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GEOPETRO RESOURCES COMPANY

UNAUDITED CONSOLIDATED STATEMENTS OF OPERATIONS

	Three Months Ended September 30, 2009	Three Months Ended September 30, 2008	Nine months Ended September 30, 2009	Nine months Ended September 30, 2008
Revenues:				
Natural gas sales	$ 973,653	$ 1,313,308	$ 2,919,923	$ 6,106,898
Costs and expenses:				
Plant operating expense	1,396,346		3,749,484	
Lease operating expense	93,773	296,927	478,187	1,287,309
General and administrative	561,227	601,757	2,026,821	1,921,270
Net profits interest		112,308		601,237
Impairment expense	939,703		939,703	63,766
Depreciation and depletion expense	432,559	343,364	1,159,050	1,326,099
Total costs and expenses	3,423,608	1,354,356	8,353,245	5,199,681
Income (loss) from operations	(2,449,955)	(41,048)	(5,433,322)	907,217
Other Income and (Expense):				
Interest expense	(163,645)		(563,991)	
Interest income	976	25,741	4,949	73,609
Gain on sale of equipment	1,488,687		1,488,687	
Total other income (expense)	1,326,018	25,741	929,645	73,609
Income (Loss) Before Taxes	(1,123,937)	(15,307)	(4,503,677)	980,826
Income tax (expense) benefit	2,836	(335)	991	(15,630)
Net Income (Loss)	(1,121,101)	(15,642)	(4,502,686)	965,196
Dividend	(43,871)		(68,583)	
Net Income (Loss) Available to Common Shareholders	$ (1,164,972)	$ (15,642)	$ (4,571,269)	$ 965,196
Earnings (Loss) per Share:				
Basic	$ (0.03)	$ (0.00)	$ (0.13)	$ 0.03
Diluted	$ (0.03)	$ (0.00)	$ (0.13)	$ 0.03
Weighted Average Number of Common Shares Outstanding:				
Basic	34,284,646	32,783,736	34,284,646	32,413,979
Diluted	34,284,646	32,783,736	34,284,646	33,045,931

See accompanying notes to these unaudited consolidated financial statements.

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GEOPETRO RESOURCES COMPANY

UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS

	For the Nine Months Ended September 30, 2009	September 30, 2008
Cash Flows From Operating Activities:		
Net income (loss)	$ (4,502,686)	$ 965,196
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation and depletion	1,159,050	1,326,099
Share-based compensation expense	299,133	165,408
Non-cash interest expense	37,849	
Impairment expense	939,703	63,766
Gain on sales of assets	(1,488,687)	
Accretion of discount on asset retirement obligations	3,503	3,185
Changes in operating assets and liabilities:		
Accounts receivable - natural gas sales	(274,598)	819,125
Other assets	82,663	183,604
Current liabilities	393,236	119,018
Net cash provided by (used in) operating activities	(3,350,834)	3,645,401
Cash Flows from Investing Activities:		
Additions to oil and gas properties	(678,352)	(5,345,519)
Additions to gas treatment plant	(83,097)	
Acquisition of furniture, fixtures & equipment		(4,305)
Dispositions of equipment	2,500,000	
Net cash provided by (used in) investing activities	1,738,551	(5,349,824)
Cash Flows from Financing Activities:		
Proceeds from sale of common shares, option and warrant exercises, net		375,000
Proceeds from sale of preferred stock Series B, net	3,031,710	
Proceeds from promissory notes	1,177,000	
Payments of loan fee	(15,200)	
Repayments of notes payable	(1,707,000)	
Net cash provided by financing activities	2,486,510	375,000
Net Increase (Decrease) in Cash and Cash Equivalents:	874,227	(1,329,423)
Cash and Cash Equivalents:		
Beginning of period	770,779	4,294,565
End of period	$ 1,645,006	$ 2,965,142
Supplemental Disclosure of Cash Flow Information:		
Cash paid for interest	$ 412,769	$
Cash paid for income taxes	$ (991)	$ 15,630

See accompanying notes to these unaudited consolidated financial statements.

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GEOPETRO RESOURCES COMPANY

UNAUDITED STATEMENT OF SHAREHOLDERS EQUITY

	Preferred Stock Series B		Preferred Stock Series AA		Common Stock		Additional Paid-in	Accumulated	Total Shareholders
	Shares	Amount	Shares	Amount	Shares	Amount	Captial	Deficit	Equity
Balances, December 31, 2008		$		$	34,284,646	$ 53,397,733	$ 2,610,596	$ (12,185,614)	43,822,715
Issuance of preferred stock Series B for cash, net from private placement	4,121,004	3,031,710							3,031,710
Fair market value of the options							299,133		299,133
Fair market value of the warrants related to notes							27,010		27,010
Net Income								(4,502,686)	(4,502,686)
Dividends on Series B Preferred Stock								(68,583)	(68,583)
Balances, September 30, 2009	4,121,004	$ 3,031,710		$	34,284,646	$ 53,397,733	$ 2,936,739	$ (16,756,883)	$ 42,609,299

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GEOPETRO RESOURCES COMPANY

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

1. BASIS OF PRESENTATION AND USE OF ESTIMATES:

The interim consolidated financial statements of GeoPetro Resources Company (we, us, our, GeoPetro or the Company) are unaudited and contain all adjustments (consisting primarily of normal recurring accruals) necessary for a fair statement of the results for the interim periods presented. Results for interim periods are not necessarily indicative of results to be expected for a full year or for previously reported periods due in part, but not limited to, the volatility in crude oil and natural gas commodity prices, interest rates, estimates of reserves, drilling risks, geological risks, transportation restrictions, the timing of acquisitions, product demand, market competition, interruption in production and our ability to obtain additional capital. You should read these consolidated interim financial statements in conjunction with the audited consolidated financial statements and notes thereto included in GeoPetro s Annual Report on Form 10-K for the year ended December 31, 2008.

The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) and include the accounts of GeoPetro and its wholly-owned subsidiaries. Intercompany accounts and transactions are eliminated. In preparing the accompanying financial statements, management has made certain estimates and assumptions that affect reported amounts in the financial statements. Actual results may differ from those estimates. Significant assumptions are required in the valuation of proved oil and natural gas reserves, which may affect the amount at which oil and natural gas properties are recorded. The computation of share-based compensation expense requires assumptions such as volatility, expected life and the risk-free interest rate. It is at least reasonably possible these estimates could be revised in the near term, and these revisions could be material.

Change in Accounting Method and Basis of Presentation - Revenue Recognition Prior to December 31, 2008, revenue was recognized upon delivery of oil and gas production and was shown net of applicable royalty payments, as well as processing, gathering, transportation and marketing fees. The Company recognized revenue from the Madisonville Field net of applicable fees to gather, treat, transport and market the Company s natural gas production. The applicable fees were paid to unrelated third parties. On December 31, 2008, the Company completed the acquisition of the Plant from Madisonville Gas Processing, LP (MGP). As of January 1, 2009, revenue is being recognized without the netting of applicable royalty payments, as well as processing, gathering, transportation and marketing fees since we have acquired the Plant. For all periods presented, revenue from the Madisonville Field is recognized when the price for gas delivered became fixed and determinable.

Impairment of Oil and Gas Properties Under full cost accounting, a ceiling test is performed to ensure that unamortized capitalized costs in each cost center (country) do not exceed their fair value. Impairment is recognized when the carrying value is greater than the discounted future cash flows. In the event of impairment, the amount by which the carrying value exceeds the estimated fair value of the long-lived asset is charged to earnings. The present

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value of estimated future net revenues is computed by applying current oil and gas prices to estimated future production of proved oil and gas reserves as of period-end, less estimated future expenditures to be incurred in developing and producing the proved reserves assuming the continuation of existing economic conditions. We recognized no impairment of evaluated properties at September 30, 2009. Under current accounting rules, we are required to use the natural gas price prevailing on the last day of our accounting period to determine whether any impairment needs to be recognized. However, we are permitted in certain circumstances to use a price that is in effect subsequent to our period end but prior to the issuance of our financial statements. In determining that no impairment existed at September 30, 2009, we utilized the price prevailing on October 30, 2009 to determine that the carrying value of the unamortized capitalized costs in our United States cost center did not exceed the discounted future cash flows from those properties. Had we used the price prevailing on September 30, 2009, we would have recognized an impairment expense of $7,921,708.

2. LIQUIDITY:

As of September 30, 2009, we have a working capital deficit of $2,716,389, and for the nine months ended, our cash used in operating activities amounted to $3,350,834. We estimate our minimum investment needs during (i) the remainder of 2009 and (ii) calendar 2010, amount to $4,500,000 related to our natural gas processing plant and our natural gas properties within the Madisonville field. Our results of natural gas operations amounted to a deficit of $4,571,269 for the nine months ended September 30, 2009. Further, we have debt service and dividend requirements that will require cash payments. We hold working interests in undeveloped leases, seismic options, lease options and foreign concessions and we have participated in seismic surveys and the drilling of test wells on undeveloped properties. We plan further leasehold acquisitions and seismic operations for the remainder of 2009 and future periods. Exploratory and developmental drilling is scheduled during 2010 and future periods on our undeveloped properties. During the nine months ended September 30, 2009, we raised $850,000 in convertible notes that were converted into our Series B Preferred Stock on April 30, 2009, an additional $2,181,710 in our Series B Preferred Stock, and issued $1,177,000 in promissory notes. On September 30, 2009, we completed the sale of certain idle equipment from our natural gas processing plant for total cash proceeds of $2.5 million. During October 2009, we issued a promissory note for total gross proceeds of $720,000 (net proceeds of $691,200) and issued an additional 3,395,000 shares of Series B Preferred Stock for total gross proceeds of $2,546,250. In addition to these items, we will need to raise additional equity or enter into new borrowing arrangements to finance our operating deficit and our continued participation in planned activities. If additional financing is not available, we will be compelled to reduce the scope of our business activities. If we are unable to fund our operating cash flow needs and planned capital investments, it will be necessary to farm-out our interest in proposed wells, sell a portion of our interest in prospects, sell a portion of our interest in our producing oil and gas properties, reduce general and administrative expenses, or a combination of all of these factors.

3. RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS:

In December 2007, the FASB issued ASC 805-10 (formerly SFAS No. 141 (revised 2007)), *Business Combinations*. ASC 805-10, which among other things, establishes principles and requirements for how the acquirer in a business combination (i) recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, and any noncontrolling interest in the acquired business, (ii) recognizes and measures the goodwill acquired in the business combination or a gain from a bargain purchase, and (iii) determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination. ASC 805-10 is effective for fiscal years beginning on or after December 15, 2008, with early adoption prohibited. This standard will change our accounting treatment for business combinations on a prospective basis.

In December 2007, the FASB issued ASC 810-10 (formerly SFAS No. 160), *Noncontrolling Interests in Consolidated Financial Statements, an Amendment of ASC 860-10 (formerly ARB No. 51)*. ASC 810-10 establishes accounting and reporting standards for noncontrolling interests in a subsidiary and for the deconsolidation of a subsidiary. Minority interests are recharacterized as noncontrolling interests and classified as a component of equity. It also establishes a single method of accounting for changes in a parent s ownership interest in a subsidiary and requires

expanded disclosures. This statement is effective for fiscal years beginning on or after December 15, 2008, with early adoption prohibited. The adoption of ASC 810-10 on January 1, 2009 did not have a material impact on our financial position or results of operations.

In March 2008, the FASB issued ASC 815-10 (formerly SFAS No. 161), *Disclosures about Derivative Instruments and Hedging Activities*, an amendment of FASB Statement No. 133. ASC 815-10 amends and expands the disclosure requirements of FASB Statement No. 133 with the intent to provide users of financial statement with an enhanced understanding of (i) how and why an entity uses derivative instruments, (ii) how derivative instruments and the related

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hedged items are accounted for under FASB Statement No. 133 and its related interpretations, and (iii) how derivative instruments and related hedged items affect and entity s financial position, financial performance and cash flows. The adoption of ASC 815-10 on January 1, 2009 did not have a material impact on our reported financial position or results of operations.

In June 2008, the FASB ratified the consensus reached on ASC 815-40 (formerly Emerging Issues Task Force (EITF) Issue No. 07-05), Determining Whether an Instrument (or Embedded Feature) Is Indexed to an Entity s Own Stock. ASC 815-40 clarifies the determination of whether an instrument (or an embedded feature) is indexed to an entity s own stock, which would qualify as a scope exception under ASC 815-10, Accounting for Derivative Instruments and Hedging Activities. ASC 815-40 is effective for financial statements issued for fiscal years beginning after December 15, 2008. Early adoption for an existing instrument is not permitted. The adoption of ASC 815-40 on January 1, 2009 did not have a material effect on our consolidated financial statements.

In December 2008, the SEC issued the final rule on the Modernization of Oil and Gas Reporting. This SEC ruling revises its oil and gas reserves reporting requirements effective for fiscal years ending on or after December 31, 2009, with early adoption prohibited. These revisions by the SEC are intended to provide investors with a more meaningful and comprehensive understanding of oil and gas reserves. These changes include:

- Modifying prices used to estimate reserves for SEC disclosure purposes to a 12-month average price instead of a single-day, period-end price.

- Requiring certain additional disclosures around proved undeveloped reserves, internal controls used to ensure objectivity of the estimation process, and qualifications of those preparing and/or auditing the reserves.

- Expanding the definition of oil and gas reserves and providing clarification of certain concepts and technologies used in the reserve estimation process.

- Allowing optional disclosure of probable and possible reserves and permitting optional disclosure of price sensitivity analysis.

Historically, the reserves calculated based on the SEC s reporting requirements were also used to calculate depletion on our producing properties, as required by ASC 932-235 (formerly SFAS 69) Disclosures about Oil and Gas Producing Activities . However, the change in the SEC reporting requirements has not yet been adopted by the FASB. The SEC has announced its intent to discuss potential amendments to ASC 932-235 with the FASB so that the reserves disclosed remain consistent with the reserves used to calculate depletion on our producing properties. Any such change would impact our future financial results. The SEC has indicated that it may delay the effective date of the revised reporting requirements if the FASB does not make conforming amendments by December 31, 2009.

On June 30, 2009, we adopted ASC 855-10 (formerly SFAS No. 165) *Subsequent Events*. ASC 855-10 establishes general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued or are available to be

issued. Specifically, ASC 855-10 sets forth the period after the balance sheet date during which management of a reporting entity should evaluate events or transactions that may occur for potential recognition or disclosure in the financial statements, the circumstances under which an entity should recognize events or transactions occurring after the balance sheet date in its financial statements, and the disclosures that an entity should make about events or transactions that occurred after the balance sheet date. The adoption of ASC 855-10 had no impact on our results, cash flow or financial position as management already followed a similar approach prior to the adoption of this standard.

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4. EARNINGS (LOSS) PER COMMON SHARE:

Basic net loss per common share is computed by dividing the net loss attributable to common shareholders by the weighted average number of shares of common stock outstanding during the period.

Diluted net loss per common share is computed in the same manner, but also considers the effect of common stock shares underlying the following:

	For the nine months ended	
	September 30, 2009	September 30, 2008
Stock options (Note 8)	2,720,000	2,740,000
Warrants (Note 9)	1,342,857	2,141,855
Convertible Preferred Stock, Series B	4,121,004	

All of the common shares underlying the stock options, warrants and convertible preferred stock, Series B above were excluded from diluted weighted average shares outstanding for the three and nine months ended September 30, 2009 and three months ended September 30, 2008 because their effects were antidilutive.

The following is a reconciliation of the numerator and denominator of our basic and diluted earning per share for the nine months ended September 30, 2008.

	Nine months ended September 30, 2008					
	Income (numerator)		Shares (denominator)		Per-share amount	
Basic earnings per share:						
Net income	$	965,196		32,413,979	$	0.03
Effective of dilutive securities:						
Share-based compensation, treasury method				631,952		
Net income plus assumed conversions	$	965,196	$	33,045,931	$	0.03

5. GAS PROCESSING PLANT

On December 31, 2008, the Company completed the acquisition of a natural gas treatment plant (the Plant) from MGP, in exchange for shares of GeoPetro s common stock, assumption of debt and a cash payment (the Acquisition). The Plant is located in Madison County, Texas and the new owner of the Plant is GeoPetro s wholly-owned indirect subsidiary, Madisonville Midstream LLC (MM).

Our results of operations for the three and nine months ended September 30, 2009 include the operating results of the Plant. However, our results of operations for the three and nine months ended September 30, 2008 do not include the operating results of the natural gas treatment plant because such acquisition closed on December 31, 2008. The following condensed pro forma information gives effect to the acquisition as if it had occurred on January 1, 2008. The pro forma information has been included in the notes as required by generally accepted accounting principles and is provided for comparison purposes only. The pro forma financial information is not necessarily indicative of the financial results that would have occurred had the acquisition been effective on the dates indicated and should not be viewed as indicative of operations in the future.

	Three Months Ended September 30, 2008	Nine Months Ended September 30, 2008
Operating revenues	$ 3,089,035	$ 13,841,215
Total operating expenses	$ 3,743,496	$ 13,102,514
Earnings (loss) applicable to common stock	$ (512,468)	$ 492,921
Net earnings (loss) per share - basic	$ (0.02)	$ 0.01
Net earnings (loss) per share - diluted	$ (0.02)	$ 0.01

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6. DEBT*:*

Debt at September 30, 2009 and December 31, 2008 consisted of the following:

	September 30, 2009	December 31, 2008
Promissory notes dated December 23, 2008 (a)	$ 1,050,000	$ 1,050,000
Promissory notes dated May 2009(b)	365,000	
Promissory notes dated June 2009(c)	300,000	
Bridge notes dated August and September 2009(d)	380,000	
Bank of Oklahoma loan (e)	5,122,847	6,697,847
	7,217,847	7,747,847
Less current portion of long term debt	(1,280,000)	(600,000)
Less discount on promissory notes	(107,340)	(128,398)
	$ 5,830,507	$ 7,019,449

(a) The Company issued four promissory notes totaling $1,050,000 during December 2008 with maturity dates in December 2011. The notes may be repaid at any time without penalty. The notes bear an annual rate of eight percent (8%), with such interest payable quarterly in arrears. The principal amount and accrued and unpaid interest are due and payable on December 23, 2011. In connection with the notes, the Company paid loan origination fees totaling $6,000 and granted three-year exercisable warrants to purchase 105,000 Common Shares and reissued 15,000 warrants at $1.00 per share. We also issued 150,000 warrants as a finder s fee. The fair value of the warrants on the dates of issuance, $122,764 and the $6,000 of loan origination fees, was recorded as a debt discount and is being amortized over the life of the promissory note. As of September 30, 2009, the unamortized debt discount was $96,207.

(b) During the nine months ended September 30, 2009 the Company borrowed $365,000 pursuant to two separate three-year loans. The notes have maturity dates in May 2012. The notes may be repaid at any time without penalty. The notes bear an annual rate of eight percent (8%), with such interest payable quarterly in arrears. The principal amount and accrued and unpaid interest are due and payable on May 2012. In connection with the notes, the Company granted three-year exercisable warrants to purchase 36,500 Common Shares warrants at $1.00 per share. The fair value of the warrants on the dates of issuance, $12,724, was recorded as a debt discount and is being amortized over the life of the promissory note. As of September 30, 2009, the unamortized debt discount was $12,194.

(c) In June 2009 the Company borrowed $300,000 pursuant to two separate one-year loans. The two notes have maturity dates in May 2010. The notes may be repaid at any time without penalty. The notes bear an annual rate of eight percent (8%), with such interest payable quarterly in arrears. The principal amount and accrued and unpaid interest are due and payable on May 2010. In connection with the notes, the Company granted three-year exercisable warrants to purchase 30,000 Common Shares warrants at $1.00 per share. The fair value of the warrants on the dates of issuance, $7,537, was recorded as a debt discount and is being amortized over the life of the promissory note. As of September 30, 2009, the unamortized debt discount was $5,652.

(d) During August and September 2009, the Company borrowed $380,000 pursuant to four separate one-year bridge loans. The notes have maturity date in August 31, 2010. The notes may be repaid at any time without penalty. The note bears an annual rate of ten percent (10%), with such interest payable at maturity. The principal amount and accrued and unpaid interest are due and payable on August 31, 2010. In

connection with the notes, the Company granted three-year warrants exercisable to purchase 14,000 Common Shares at $1.00 per share. The fair value of the warrants on the dates of issuance, $6,750, was recorded as a debt discount and is being amortized over the life of the bridge note. As of September 30, 2009, the unamortized debt discount was $6,082. On October 6, 2009, we repaid one of the bridge notes in the principal amount of $100,000 plus accrued interest.

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(e) Effective December 31, 2008, the Company assumed $7,697,847 of Madisonville Gas Processing LP s (MGP) bank debt related to the Company s acquisition of the Madisonville Gas Treatment Plant (the Plant) via a (i) $1 million cash payment applied directly towards debt principal reduction, and (ii) a refinancing by GeoPetro of the $6,697,847 remaining balance in the form of a 3 year Amended and Restated Term Loan Agreement with the lender, Bank of Oklahoma (BOK). The terms of the three year loan provide for minimum quarterly principal payments of $150,000 and interest payable quarterly in arrears at prime plus 4% or Libor plus 5.5% at the option of the Company. At September 30, 2009, the interest rate was approximately 6% (LIBOR + 5.5%). Additional principal will be payable upon GeoPetro meeting certain net operating cash flow thresholds during the three year term of the loan. The loan is secured by a first lien on the Madisonville Midstream Plant and all of the Company s proved natural gas reserves located at the Madisonville Project. In addition, GeoPetro has agreed to pay, at the time the loan is repaid in full, a loan origination fee of $60,000 for any annual period during which the loan principal remains outstanding. There is no prepayment penalty. The Amended and Restated Term Loan Agreement contains customary affirmative and negative covenants including restrictions on incurring additional debt and requiring that the Company maintain a minimum tangible net worth of at least $35,000,000. On September 30, 2009, GeoPetro sold certain idle equipment to an unrelated party in the amount of $2.5 million. GeoPetro used a portion of the proceeds to repay $1.125 million principal to Bank of Oklahoma.

7. INCOME TAXES:

The Company files income tax returns in the U.S. federal jurisdiction and various states. There are currently no federal or state income tax examinations underway. Furthermore, the Company is no longer subject to U.S. federal income tax examinations by the Internal Revenue Service for tax years before 2005 and for state and local tax authorities for tax years before 2004. The Company does, however, have net operating losses generated in tax years 1997 and after, which remain open for examination.

The Company adopted the provisions of ASC 740-10 (formerly FASB Interpretation No. 48), Accounting for Uncertainty in Income Taxes, on January 1, 2007. As of December 31, 2008 the Company had no unrecognized tax benefits. There have been no changes during the year with respect to unrecognized tax benefits. The Company does not foresee the total amounts of unrecognized tax benefits significantly increasing within the next 12 months. Furthermore, no corresponding interest and penalties have been accrued as the Company is in a net operating loss position.

The Company provides for income taxes in accordance with ASC 740-10 (formerly Statement of Financial Accounting Standards No. 109, Accounting for Income Taxes. ASC 740-10 requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the financial statement carrying amounts and the tax basis of the assets and liabilities. Where it is more likely than not that a tax benefit will not be realized, a valuation allowance is recorded to reduce the deferred tax asset to its realizable value.

A valuation allowance has been provided against the Company s net deferred tax assets as the Company believes that it is more likely than not that the net deferred tax assets will not be realized.

The effective tax rate for the nine month period ended September 30, 2009 was 0%, and for the year ended December 31, 2008 was (7.9) percent, and differs from statutory rates primarily due to changes in the valuation allowance.

8. COMMON STOCK OPTIONS:

There were no material changes to common stock options from those disclosed in the audited annual consolidated financial statements for the year ended December 31, 2008 except the following.

On June 26, 2009, the Company granted a total of 60,000 5 year options to four non-management directors. The weighted average fair value of options granted as calculated under the Black-Scholes pricing model was $0.33 per share with the following weighted-average assumptions: risk-free, weighted-average interest rate of 2.53 percent based on the U.S. Treasury yield curve in effect at the time of grant, expected dividend yield of 0 percent, expected life of 5 years from the date of grant, and expected volatility of 113 percent based on the Company s historical daily stock trading since February 16, 2007.

On April 27, 2009, the Company reduced the option price previously granted to an officer from $2.10 per share to $1.00 per share based on the new employment agreement. The fair value of the repricing options was insignificant.

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The options outstanding as of September 30, 2009 have the following contractual lives:

Number of Options Outstanding	Number of Options Exercisable	Exercise Prices	Weighted Average Remaining Contractual Life
210,000	150,000	1.00	4.51
1,600,000	1,600,000	2.10	3.68
150,000	90,000	3.85	1.54
10,000	8,000	4.25	0.25
740,000	148,000	4.28	3.74
10,000	8,000	6.25	0.69
2,720,000	2,004,000		

The total intrinsic value of options outstanding was approximately $0 and $332,500 at September 30, 2009 and 2008 respectively. The intrinsic value for exercisable options was $0 and $332,500 at September 30, 2009 and 2008, respectively.

As of September 30, 2009, there are 2,004,000 options which are exercisable. The remaining 716,000 options will become exercisable over the next four years. The stock compensation expense related to the unvested awards is $1,305,418.

9. COMMON STOCK WARRANTS*:*

On April 10, 2009, the Company extended the expiration date on a warrant to purchase 114,000 shares of common stock (exercisable at $3.50 per share) to December 15, 2011. The fair value of the warrant extension was insignificant.

On March 31, 2009, the Company extended the expiration date on a warrant to purchase 100,000 shares of common stock (exercisable at $5.25 per share) to March 31, 2014. The fair value of the warrant extension was insignificant.

On February 23, 2009, the Company issued 50,000 shares of the common stock warrants to a non-related party expiring February 22, 2012 with a strike price of $1.00 per share. Warrants granted shall vest according the following schedule: 25% immediately; 25% at the three month anniversary of the signing of the agreement; 25% at the six month anniversary of the signing of the agreement; and 25% at the nine month anniversary of the signing of the agreement. The grant-date fair value of the warrants amounted to $8,106, using the Black-Scholes valuation method, which is recognized in general and administrative expense on our consolidated statement of operations ratably over the requisite service period as defined by the vesting schedule above.

10. GAIN ON SALE OF EQUIPMENT*:*

On September 10, 2009, the Company s subsidiary, Madisonville Midstream, LLC entered into an agreement to sell certain idle equipment related to the plant to an unrelated third party, Gas Processors, Inc., for a purchase price of $2.5 million. A nonrefundable deposit of $250,000 was received on September 10, 2009 and the remaining balance of $2.25 million was tendered to Madisonville Midstream on the closing date of September 30, 2009. Concurrent with the receipt of the sales proceeds, the Company paid $1,125,000 to reduce the principal balance on the Bank of Oklahoma loan. The Company recorded a gain of $1,488,687 on the sale.

11. COMMITMENTS AND CONTINGENCIES:

There are no material changes to commitments and contingencies from those disclosed in the audited annual consolidated financial statements for the year ended December 31, 2008.

On September 11, 2009, the Company s subsidiary, Redwood Energy Production, L.P. filed an Original Petition for Declaratory Judgment against Devon Energy Production Company (Devon) regarding certain overriding royalty interests and related revenue amounts claimed by Devon. The Company previously accrued all amounts owed pursuant to these overriding royalty interests as royalty owners payable. In the opinion of management based on consultation with legal counsel, these proceedings are not expected to have a material adverse effect on our financial condition or results of operations.

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12. SUBSEQUENT EVENTS THROUGH NOVEMBER 9, 2009.

On October 23, 2009, we issued a promissory note for total gross proceeds of $720,000 (net proceeds of $691,200). The note has a maturity date of October 31, 2010 and bears interest at 10% per annum, payable at maturity. We issued to the note holder warrants exercisable to purchase 36,000 shares of our common stock. Each warrant is exercisable for a three year term to purchase one share of our common stock at a price of $1.00 per share.

On October 8, 2009, the Company filed a Certificate of Amendment with the California Secretary of State for the purpose of amending its Articles of Incorporation to increase the total number of authorized shares of Series B Preferred Stock from 6,800,000 to 7,523,000 shares of Series B Preferred Stock. During October 2009, we issued an additional 3,395,000 shares of Series B Preferred Stock for total gross proceeds of $2,546,250.

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

The following discussion and analysis should be read in conjunction with accompanying financial statements and related notes included elsewhere in this report. It contains forward looking statements that reflect our future plans, estimates, beliefs and expected performance. The forward looking statements are dependent upon events, risks and uncertainties that may be outside our control. Our actual results could differ materially from those discussed in these forward looking statements.

Factors that could cause or contribute to such differences include, but are not limited to, market prices for natural gas and oil, economic and competitive conditions, regulatory changes, estimates of proved reserves, potential failure to achieve production from development drilling projects, capital expenditures and other uncertainties, as well as those factors discussed below and elsewhere in this report, particularly in Risk Factors , all of which are difficult to predict and which expressly qualify all subsequent oral and written forward-looking statements attributable to us or persons acting on our behalf. In light of these risks, uncertainties and assumptions, the forward looking events discussed may not occur. We do not have any intention or obligation to update forward-looking statements included in this report after the date of this report, except as required by law.

Overview

We are an oil and gas company in the business of exploring and developing oil and natural gas reserves on a worldwide basis. Since inception, we have conducted leasehold acquisition, exploration and drilling activities on our North American, Australian and Indonesian prospects. These projects currently encompass approximately 379,547 gross (161,171 net) acres, consisting of mineral leases, production sharing contracts and exploration permits that give us the right to explore for, develop and produce oil and natural gas. Most of these properties are in the exploration, appraisal or development drilling phase and have not begun to produce revenue from the sale of oil and natural gas. Excluding minor interest and dividend income, our only significant cash inflows until 2003 were the recovery of capital invested in projects through sale or other divestiture of interests in oil and gas prospects to industry partners.

Since 2003, substantially all of our revenue has been generated from natural gas sales derived from the Magness #1, the Fannin #1, and the Mitchell #1 wells in the Madisonville Field in East Texas under spot gas purchase contracts at market prices. Natural gas sales from the Madisonville Field are expected to account for substantially all of our revenues for 2009. We expect the majority of our capital expenditures in 2009 and 2010 will be for the Madisonville Project.

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Results of Operations

The financial information with respect to the nine months ended September 30, 2009 and 2008 that is discussed below is unaudited. In the opinion of management, such information contains all adjustments, consisting only of normal recurring accruals, necessary for a fair presentation of the results for such periods. The results of operations for interim periods are not necessarily indicative of the results of operations for the full fiscal years.

	Nine Months Ended	
	September 30, 2009 (unaudited)	September 30, 2008 (unaudited)
Consolidated Statement of Operations:		
Revenues	$ 2,919,923	$ 6,106,898
Plant operating expense	3,749,484	
Lease operating expense	478,187	1,287,309
General and administrative	2,026,821	1,921,270
Net profits expense		601,237
Impairment expense	939,703	63,766
Depreciation and depletion expense	1,159,050	1,326,099
Earnings (loss) from operations	(5,433,322)	907,217
Net income (loss)	(4,502,686)	965,196
Net income (loss) attributable to common shareholders	(4,571,269)	$ 965,196

Revenue and Operating Trends in 2009

We developed an onsite plan to treat and remove impurities from the Madisonville Project natural gas in order to meet pipeline-quality specifications. The Madisonville Project is located in East Texas. In 2003, the construction and installation of a natural gas treatment plant with a designed capacity of 18 million cubic feet of gas per day (MMcf/d) and associated pipeline and gathering facilities were completed. The treatment plant and associated gathering facilities were owned by an unaffiliated third party.

In 2005 we secured a commitment from MGP to install and make operational additional treating facilities capable of treating 50 MMcf/d, which combined with the capacity of the current in-service treating facilities will represent a total designed treating capacity of 68 MMcf/d for the Madisonville treatment plant. In early November 2007, MGP began testing the additional treatment facilities by accepting 20 MMcf/d at the inlet. Subsequently in December 2007, MGP temporarily suspended the operations of the additional treatment facilities in order to make modifications to more effectively deal with the presence of diamondoids in the gas stream produced from the Rodessa Formation.

During 2008, MGP analyzed various options for removing the diamondoids; however, they did not complete the