

CASTLEGUARD ENERGY INC  
Form 10KSB  
March 30, 2004

-----  
UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-KSB

(MARK  
ONE)

- ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES AND EXCHANGE ACT OF 1934 FOR THE FISCAL YEAR ENDED DECEMBER 31, 2003
- TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE TRANSITION PERIOD FROM \_\_\_\_\_ TO \_\_\_\_\_

COMMISSION FILE NUMBER: 0-5525

CASTLEGUARD ENERGY, INC.  
(Exact name of Registrant as specified in its charter)

Florida  
(State or other jurisdiction of  
of incorporation or organization)

75-2789691  
(I.R.S. Employer  
Identification No.)

4625 Greenville Avenue, Suite 203, Dallas, TX  
(Address of principal executive offices)

75206  
(Zip Code)

(214) 361-1755  
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act: NONE

Securities registered pursuant to Section 12(g) of the Act:  
Common Stock Without Par Value  
(Title of Class)

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

Edgar Filing: CASTLEGUARD ENERGY INC - Form 10KSB

(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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-B is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-KSB or any amendment to this Form 10-KSB.

State the registrant's revenues for its most recent fiscal year: \$ 486,894

The aggregate market value on March 15, 2004, of Common shares held by non-affiliates was approximately \$729,259 based on the average closing bid and asked prices of the registrant's Common shares on such date, as quoted by the National Quotation Bureau.

At March 15, 2004, there were 17,364,626 Common shares outstanding.

---

Transitional Small Business Disclosure Format (check one): Yes  No

CASTLEGUARD ENERGY, INC.

2003 FORM 10-KSB ANNUAL REPORT

Table of Contents

Part I.

- Item 1. Description of Business
  - (a) General Business Description
  - (b) Description of Business - Oil and Gas Operations

Item 2. Description of Properties

Item 3. Legal Proceedings

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

Part II.

Item 5. Market for Common Equity and Related Stockholder Matters

- Item 6. Management's Discussion and Analysis or Plan of Operation
- Item 7. Financial Statements
- Item 8. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure
- Item 8A. Controls and Procedures

Part III.

- Item 9. Directors, Executive Officers, Promoters and Control Persons; Compliance With Section 16(a) of the Exchange Act
- Item 10. Executive Compensation
- Item 11. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters
- Item 12. Certain Relationships and Related Transactions
- Item 13. Exhibits and Reports on Form 8-K
- Item 14. Principal Accountant Fees and Services

Signature Page

Appendix A Financial Information

F-1

PART I

-----

ITEM 1 - DESCRIPTION OF BUSINESS

-----

(a) GENERAL BUSINESS DESCRIPTION

-----

GENERAL

Castleguard Energy, Inc. (the "Company") is an independent energy company engaged in the exploration for and the acquisition, development, exploitation and operation of crude oil and natural gas properties, and in the production of crude oil and natural gas in North America. The Company's activities are conducted principally in the States of Louisiana, Texas and Alabama.

The Company acquires interests in land and producing properties through acquisition and lease on which it drills and/or has working interests in oil or gas wells in efforts to discover and/or to produce oil and gas.

The Company's executive offices are located at 4625 Greenville Avenue, Suite 203, Dallas, Texas 75206 , telephone (214) 361-1755, facsimile (214) 691-2230.

(b) DESCRIPTION OF BUSINESS - OIL AND GAS OPERATIONS

-----  
Exploration and Development  
-----

The Company operates in a highly competitive industry wherein many companies, from large multinational companies to small independent producers, are competing for a finite amount of oil and gas resources. The Company seeks out properties to explore for oil and gas by drilling and also seeks out producing oil and gas properties that can be purchased.

Management believes that under the right economic conditions, several of the producing properties that the Company owns could have further developmental potential. Certain oil properties currently owned and operated by the Company may be receptive to enhanced oil recovery procedures.

Operating Activities

The Company contracts with other parties, including officers, directors, principal stockholders or other affiliates of the Company, to act as operator of the oil and gas prospects in which it owns an interest, provided such transactions are on terms and conditions substantially similar to those offered by nonaffiliated parties. The operator of an oil and gas property supervises production, maintains production records, employs field personnel and performs other functions required in the production and administration of such property. The fees for such services customarily vary from well to well, depending on the nature, depth and location of the well being operated. Generally, the operator of an oil and gas prospect is determined by such factors as the size of the working interest held by a participant in the prospect, a participant's knowledge and experience in the geological area in which the prospect is located and geographical considerations. The Company's wells are drilled by independent drilling contractors.

Developments During Year 2003

The Company's operating activities, carried out by the operators of oil and gas properties in which Castleguard has an interest, included participating in the following:

-

Experienced a significant decline in production during 2003 from two Minden gas wells worked over in late 2002 to address mechanical problems that developed late in the third quarter of 2002 and which had sharply curtailed gas production. Reserves at year end 2003 were also lowered sharply from the production decline;

- Louisiana Conservation Commission reduced Castleguard's interest in certain sands of the Youngblood 21-1D well in the Minden field retroactive to the date of first production, resulting in a \$83,631 payment to another producer, which was treated as an addition to the fixed asset pool because the periods involved were prior to acquisition of Castleguard's interest;
- Farmed-out a 1/16 interest in a new well to be drilled in Minden, retaining a .0375 interest in the well with the right to receive a 20% interest in the farmout after payout;
- Drilling of a new well in the Minden field which showed several potential producing formations but which was pending final completion at the end of February 2004.

#### Disclosure Regarding Forward-Looking Statements And Cautionary Statements

##### Forward-Looking Statements

This Annual Report on Form 10-KSB includes "forward-looking" statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). All statements other than statements of historical facts included in this Annual Report, including without limitation statements under "ITEMS 1 AND 2. DESCRIPTION OF BUSINESS AND PROPERTIES" and "ITEM 6. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION", regarding the Company's financial position, business strategy, and plans and objectives of management of the Company for future operations and capital expenditures, are forward-looking statements. Although the Company believes that the expectations reflected in the forward-looking statements and the assumptions upon which the forward-looking statements are based are reasonable, it can give no assurance that such expectations and assumptions will prove to have been correct. Additional statements concerning important factors that could cause actual results to differ materially from the Company's expectation ("Cautionary Statements") are disclosed below in the "-Cautionary Statements" section and elsewhere in this Annual Report. All written and oral forward-looking statements attributable to the Company or persons acting on its behalf subsequent to the date of this Annual Report are expressly qualified in their entirety by the Cautionary Statements.

##### Cautionary Statements

In addition to the other information contained in this Annual Report, the following Cautionary Statements should be considered when evaluating the forward-looking statements contained in this Annual Report.

#### Nature Of The Company's Oil And Gas Business

The Company was formed in 1988, and in the last five years has altered its business and become profitable. The development of the Company's business will continue to require substantial expenditures. The Company's future financial results will depend primarily on its ability to locate hydrocarbons economically in commercial quantities, to provide drilling site and target depth recommendations resulting in profitable productive wells

and on the market prices for oil and natural gas.

#### Oil And Gas Prices: Marketability Of Production

Even if the Company is able to discover or acquire oil and gas production, of which there is no assurance, the Company's revenues, profitability and liquidity will be highly dependent upon prevailing prices for oil and natural gas. Oil and gas prices can be extremely volatile and there can be no assurance that current price levels can be sustained. Prices also are affected by actions of state and local agencies, the United States and foreign governments, and international cartels. These external factors and the volatile nature of the energy markets make it difficult to estimate future prices of oil and natural gas. Any substantial or extended decline in the price of oil and/or natural gas would have a material adverse affect on the Company's financial condition and results of operations, including reduced cash flow and borrowing capacity. All of these factors are beyond the control of the Company. Sales of oil and natural gas are seasonal in nature, leading to substantial differences in cash flow at various times throughout the year. The marketability of the Company's gas production, if any, will depend in part upon the availability, proximity and capacity of gas gathering systems, pipelines and processing facilities. Federal and state regulation of oil and gas production and transportation, general economic conditions, changes in supply and changes in demand all could adversely affect the Company's ability to produce and market oil and natural gas. If market factors were to change dramatically, the financial impact on the Company could be substantial. The availability of markets and the volatility of product prices are beyond the control of the Company and thus represent a significant risk.

#### Reliance On Industry Participants

The Company attempts to limit financial exposure on a project by project basis by forming industry alliances where the Company's technical expertise can be complemented with the financial resources and operating expertise of established companies. If the Company were not able to form these industry alliances, this could limit the Company's ability to fully implement its business plan and could have a material adverse effect on the Company's business, financial condition and results of operations.

#### Ability To Discover Reserves

The Company's future success is dependent upon its ability to economically locate oil and gas reserves in commercial quantities. Except to the extent that the Company acquires properties containing proved reserves or conducts successful exploration and development activities, or both, the proved reserves of the Company, if any, will decline as reserves are produced. The Company's ability to conduct successful exploration and development activities is dependent upon a number of factors, including its participation in multiple exploration projects and its technological capability to locate oil and gas in commercial quantities. Because the Company may rely upon other industry participants to develop the Company's exploration projects, no assurances can be given that the Company will have the opportunity to participate in projects which economically produce commercial quantities of hydrocarbons in amounts necessary to meet its business plan or that the projects in which it elects to participate will be successful. There can be no assurance that the Company's planned projects will result in significant reserves or that the Company will have future success in drilling productive wells at low reserve replacement costs.

#### Substantial Capital Requirements And Liquidity

In order to continue its oil and gas exploration plans fully, the Company anticipates that it will need additional funding. The Company does not have an adequate source of revenue to provide for further exploration. There is no assurance that the Company will be able to obtain funds necessary to conduct further exploration.

#### Risk Of Exploratory Drilling Activities

Exploration for oil and natural gas is a speculative business involving a high degree of risk, including the risk that no commercially productive oil and gas reservoirs will be encountered. The cost of drilling, completing and operating wells is often uncertain and drilling operations may be curtailed, delayed or canceled as a result of a variety of factors including unexpected formation and drilling conditions, pressure or other irregularities in formations, equipment failures or accidents, as well as weather conditions, compliance with governmental requirement and shortages or delays in the delivery of equipment. There is no assurance that the expenditures made by the Company on its oil and natural gas properties will result in discoveries of oil or natural gas in commercial quantities. Some test wells, as a consequence, may not ultimately be developed into producing wells and may be abandoned.

#### Competition

The Company competes in the areas of oil and gas exploration with other companies, many of which may have substantially larger financial and other resources. From time to time, there may be competition for, and shortage of, exploration, drilling and production equipment and these shortages could lead to an increase in costs and to delays in operations that could have a material adverse effect on the Company. The Company may therefore not be able to acquire desirable properties or equipment required to develop its properties. Problems of this nature also could prevent the Company from producing any oil and natural gas it discovers at the rate it desires to do so.

#### General Risks Of Oil And Gas Operations

The nature of the oil and gas business involves a variety of risks, including the risks of operating hazards such as fires, explosions, cratering, and blowouts.

#### Technology Changes

The oil and gas industry is characterized by rapid and significant technological advancements and introductions of new products and services utilizing new technologies. As new technologies develop, the Company may be placed at a competitive disadvantage, and competitive pressures may force the Company to implement such new technologies at substantial cost. In addition, other oil and gas finding companies may implement new technologies before the Company, and consequently such companies may be able to provide enhanced capabilities and superior quality compared with that which the Company is able to provide. There can be no assurance that the Company will be able to respond to such competitive pressures and implement such technologies on a timely basis or at an acceptable cost. One or more of the technologies currently utilized by the Company or implemented in the future may become obsolete. In such case, the Company's business, financial condition and results of operations could be materially adversely affected. If the Company is unable to utilize the most advanced commercially available technology, the Company's business, financial condition and results of operations could be materially and adversely affected.

### Government Regulations And Environmental Risks

The production and sale of oil and gas are subject to a variety of federal, state and local government regulations including regulation concerning the prevention of waste, the discharge of materials into the environment, the conservation of oil and natural gas, pollution, permits for drilling operations, drilling bonds, reports concerning operations, the spacing of wells, the unitization and pooling of properties, and various other matters including taxes. Many jurisdictions have at various times imposed limitations on the production of oil and gas by restricting the rate of flow for oil and gas wells below their actual capacity to produce. During the past few years there has been a significant amount of discussion by legislators and the presidential administration concerning a variety of energy tax proposals. There can be no certainty that any such measure will be passed or what its effect will be on oil and natural gas prices if it is passed. In addition, many states have raised state taxes on energy sources and additional increases may occur, although there can be no certainty of the effect that increases in state energy taxes would have on oil and natural gas prices. Although the Company believes it is in substantial compliance with applicable environmental and other government laws and regulations, there can be no assurance that significant costs for compliance will not be incurred in the future.

### Variability Of Operating Results

The Company's operating results, as a small company in the oil and gas industry, may vary significantly during any financial period. These variations may be caused by significant periods of time between each of the Company's discoveries and developments, if any, of oil or natural gas properties in commercial quantities. These variations may also be caused by the volatility associated with oil and gas prices. See "Oil and Gas Prices; Marketability Of Production".

### Risks Associated With Management Of Growth

Because of its small size, the Company desires to grow extremely rapidly in order to achieve certain economies of scale. Although there is no assurance that this rapid growth will occur, to the extent that it does occur it will place a significant strain on the Company's financial, technical, operational and administrative resources. As the Company increases its services and enlarges the number of projects it is evaluating or in which it is participating, there will be additional demands on the Company's financial, technical and administrative resources. The failure to continue to upgrade the Company's technical, administrative, operating and financial control systems or the occurrence of unexpected expansion difficulties, including the recruitment and retention of geoscientists and engineers, could have a material adverse effect on the Company's business, financial condition and results of operations.

### Dependence On Key Personnel

The Company is highly dependent on the services of Scott Heape. The loss of the services of Mr. Heape could have a material adverse effect on the Company. The Company does not have an employment contract with Mr. Heape or any other director or officer.

### Concentration Of Risks; Lack Of Diverse Business Operations



Although the Company is involved in other oil and gas projects, it is concentrating the majority of its oil and gas exploration efforts on the Minden Dome project in Louisiana. The Company's other exploration projects are located in this same general area and this lack of diverse business operations subjects the Company to a certain degree of concentration of risks. The future success of the Company may be dependent upon its success in discovering and developing oil and gas in commercial quantities in the above properties and upon the general economic success of the oil and gas industry.

### Certain Definitions

Unless otherwise indicated in this Annual Report, natural gas volumes are stated at the legal pressure base of the state or area in which the reserves are located at 60(degree)Fahrenheit.

As used in this Annual Report, the following terms have the following specific meanings: "Mcf" means thousand cubic feet, "Bcf" means billion cubic feet, "Bbl" means barrel, "MBbl" means thousand barrels.

With respect to information concerning the Company's working interests in wells or drilling locations, "gross" gas and oil wells or "gross" acres is the number of wells or acres in which the Company has an interest, and "net" gas and oil wells or "net" acres are determined by multiplying "gross" wells or acres by the Company's working interest in those wells or acres. A "working interest" in an oil and gas lease is an interest that gives the owner the right to drill, produce, and conduct operating activities on the property and to receive a share of production of any hydrocarbons covered by the lease. A working interest in an oil and gas lease also entitles its owner to a proportionate interest in any well located on the lands covered by the lease, subject to all royalties, overriding royalties and other burdens, to all costs and expenses of exploration, development and operation of any well located on the lease, and to all risks in connection therewith.

A "development well" is a well drilled as an additional well to the same horizon or horizons as other producing wells on a prospect, or a well drilled on a spacing unit adjacent to a spacing unit with an existing well capable of commercial production and which is intended to extend the proven limits of a prospect. The latter type of development well drilling is known as "step-out drilling". An "exploratory well" is a well drilled to find commercially productive hydrocarbons in an unproved area, or to extend significantly a known prospect.

"Reserves" means natural gas and crude oil, condensate and natural gas liquids on a net revenue interest basis, found to be commercially recoverable. "Proved developed reserves" includes proved developed producing reserves and proved developed behind-pipe reserves. "Proved developed producing reserves" includes only those reserves expected to be recovered from existing completion intervals in casing of existing wells when the cost of making such reserves available for production is relatively small compared to the cost of a new well. "Proved undeveloped reserves" includes those reserves expected to be recovered from new wells on proved undrilled acreage or from existing wells where a relatively major expenditure is required for recompletion.

### Strategy

The Company's business strategy is to enhance shareholder value by leveraging its technical experience and expertise with seismic and subsurface technology to identify exploration and exploitation projects with significant potential reserves and economic results based on the application of appropriate technology and suitable project risk management. The Company's ongoing goal is to increase its reserve base through a focus

on mature hydrocarbon basins where it has expertise. It is the Company's view point that the systematic application of advanced seismic imaging and detailed subsurface work can significantly reduce drilling risk and enhance financial results. The Company's strategy is to focus on applying seismic technology to explore properties that lie within these mature basins and that offer oil and gas reserves that would be materially significant to the Company.

The Company has a two-pronged corporate approach for the application of exploration technology in these mature basins. The two components of this strategy are set forth below:

Generation of exploration and exploitation prospects with special emphasis on seismic and subsurface applications to locate structural and stratigraphic play concepts.

Networking through contacts within the industry that have proven records of exploration success.

Exploration and Operating Approach

The Company focuses its technical resources on obtaining the highest quality subsurface image through advanced geological and geophysical methods, which it believes are more likely to result in the cost effective identification of oil and gas reserves that are materially significant. The Company is committed to providing its technical team with access to the required tools and support necessary to retain a competitive advantage in today's exploration environment.

The Company adheres to a disciplined approach to selective project participation. The Company participates only in those projects that it believes are likely to maximize the return on its capital investment, have significant reserve growth potential, and have quantifiable risk /reward ratios. The Company believes that these factors result in a positive impact to the finding-cost and production economics. The Company actively and continually manages its portfolio of exploration and exploitation projects. The aggressive portfolio management enables the Company to maximize the investment of available capital in a limited number of high impact geologic plays and projects.

ITEM 2 - DESCRIPTION OF PROPERTY

-----

The Company's properties principally consist of working interests in developed oil and gas properties in Louisiana, Alabama and Texas. Developed properties are those on which sufficient wells have been drilled to economically recover the estimated reserves calculated for the property.

The Company's net proved reserves, including behind-pipe reserves, but excluding proved undeveloped reserves, as estimated by independent petroleum engineers, Gary S. Swindell & Associates , at December 31, 2003 were:

	<u>Crude Oil</u> <u>(BBLs)</u>	<u>Natural Gas</u> <u>(MCF)</u>
Proved developed producing	11,920	158,961
Proved developed non-producing	<u>1,009</u>	<u>301,774</u>

Total	<u>12,929</u>	<u>460,735</u>
-------	---------------	----------------

See Note G of the Notes to Financial Statements included in Appendix A to this report for additional information on gas and oil reserves.

At December 31, 2003, the Company owned interests in 10 gross gas wells (1.11 net), two of which are dual completions, and 3 gross oil wells (.21 net). The terms "gross" refers to the wells in which a working interest is owned, and the term "net" refers to gross wells multiplied by the percentage of Castleguard's working interest owned therein.

Castleguard participated in one producing well (in completion at year end); it participated in the recompletion of 3 wells and one dry hole in 2002.

The Company's interests in undeveloped acreage is insignificant.

#### Change in Well Ownership Interests

Through action of the Louisiana Conservation Commission, as modified by a court decision of the District of Caddo Parish, Louisiana, dated December 17, 2002, Castleguard's working interest in the Hudson Reservoir A Sand of the Youngblood 21-1D well in the Minden Field, Webster Parish Louisiana field was reduced retroactively to the date of first production. The Hudson Reservoir A Sand produced in the Youngblood 21-1D Well from December 1999 through September 2001, at which time the Hudson A Sand was abandoned and the well was recompleted in other zones. Castleguard's interest in all other producing sands in the Youngblood 21-1 Well increased slightly as a result of the Orders. After entry of the District Court's Order, the parties negotiated the methodology of implementing that decision, which resulted in a June 30, 2003 tentative agreement which was executed on behalf of Castleguard on July 12, 2003.

The reduction in Castleguard's working interest required Castleguard to pay to other working interest owners a portion of the net revenue received by Castleguard attributable to production from the Hudson A Sand and required other working interest owners to pay to Castleguard an amount for the additional share of the well costs. Calculation of the amounts owed by the parties to each other was finalized and agreed upon shortly after year-end 2003, which resulted in Castleguard paying \$83,631 in cash to another producer. The amount paid was attributed to production prior to Castleguard's acquisition of its interest, which had been treated as a reduction of purchase price at the time of acquisition. Therefore, the amount paid was treated as an addition to Castleguard's full cost pool.

#### ITEM 3 - LEGAL PROCEEDINGS

-----

The Company is not party to any proceedings or actions which management believes might have a material effect upon its financial position or results of operations.

## ITEM 4 - SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

-----

Not Applicable.

## PART II

-----

ITEM 5 - MARKET FOR COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

-----

The principal U.S. market in which the Company's Common Stock (\$.001 par value, all of which are one class) has been traded on the Over the Counter ("OTC") Bulletin Board. The Company's common stock is quoted on the OTC Bulletin Board (Symbol: "MOAT.OB"). The following table sets forth the range of high and low closing bid prices for the Company's Common Stock on a quarterly basis since January 1, 2001 as reported by the National Quotation Bureau, Inc. (which reflect inter-dealer prices, without retail mark-up, mark-down, or commission and may not necessarily represent actual transactions). As of March 15, 2004, the closing bid for the Company's common stock was \$.055 per share. The foregoing and following information should not be taken as an indication of the existence of an established public trading market for the Company's Common Stock.

<u>Quarter</u>	<u>Bid Prices</u>					
	<u>2003</u>		<u>2002</u>		<u>2001</u>	
	<u>High</u>	<u>Low</u>	<u>High</u>	<u>Low</u>	<u>High</u>	<u>Low</u>
First	\$ .08	\$ .04	\$ .11	\$ .05	\$ .28	\$ .09
Second	.06	.04	.11	.05	.28	.14
Third	.07	.04	.08	.04	.20	.06
Fourth	.08	.04	.07	.04	.13	.05

 Holders

The approximate number of record holders of the Company's Common Stock as of March 15, 2004 was 52, inclusive of those brokerage firms and/or clearing houses holding the Company's common shares for their clientele (with each such brokerage house and/or clearing house being considered as one holder). The aggregate number of shares of Common Stock outstanding as of March 15, 2004 was 17,364,626 shares, of which 11,545,213 were free trading shares.

 Dividends

Current management believes that the Company has not declared any cash dividends on its Common Stock since its inception in 1988. The Company has not declared any cash dividends on its Common Stock since current management assumed their positions in September 1998 and has no present intention of paying any cash dividends on its Common Stock in the foreseeable future.

ITEM 6 - MANAGEMENT'S DISCUSSION AND ANALYSIS OR  
PLAN OF OPERATIONS

-----

The information required hereunder is set forth under "Financial Review" included in Appendix A to this report.

ITEM 7. FINANCIAL STATEMENTS

-----

The following items appear in the Financial Information section included in Appendix A to this report.

Financial Review

Report of Independent Auditors

Financial Statements:

Balance Sheets

Statements of Income

Statements of Cash Flows

Statements of Stockholders' Equity

Notes to Financial Statements

All other schedules are omitted because they are inapplicable, not required, or the information is included in the financial statements or notes thereto.

ITEM 8. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS  
ON ACCOUNTING AND FINANCIAL DISCLOSURE.

Not Applicable.

ITEM 8A - CONTROLS AND PROCEDURES

-----

(a) Evaluation of disclosure controls and procedures

The President/Secretary/Treasurer/Director of the Company has conducted an evaluation of the effectiveness of the Company's disclosure controls and procedures pursuant to Rule 13a-14 under the Securities Exchange Act of 1934 as of the end of the period covered by this report. Based upon that evaluation, the President/Secretary/Treasurer/Director concluded that the Company's disclosure controls and procedures were effective in ensuring that all material information relating to the Company required to be filed in this annual report has been made known to them in a timely manner.

(b) Changes in internal controls

There have been no significant changes made in the Company's internal controls or in other factors that could significantly affect internal controls subsequent to the end of the period covered by this report.

PART III

-----

ITEM 9 - DIRECTORS, EXECUTIVE OFFICERS, PROMOTERS AND CONTROL PERSONS;  
COMPLIANCE WITH SECTION 16(a) OF THE EXCHANGE ACT

-----

The Company's bylaws provide that Directors are to be elected by simple majority vote and are to serve until the next annual meeting following such election or until a successor has been duly elected and qualified. Directors may be removed with or without cause by a majority vote of the stockholders and may be removed for cause by the Board. Vacancies on the board may be filled by the remaining directors or by the stockholders. The executive officers of the Company are elected by and serve at the discretion of the Board of Directors.

The following sets forth the name, and position of each director and executive officer of the Company:

<u>OFFICERS</u>	<u>AGE</u>	<u>CURRENT OFFICE</u>
Scott G. Heape	54	Chairman, Director
Bob G. Honea	66	President, Treasurer/Secretary, Director (Chief Executive and Financial Officer)
Benton J. Poole	52	Director
Harvey Jury	56	Director

Scott G. Heape

Mr. Heape is Chairman and Founder of H & S Production, Inc. and HSP Geophysical, Inc. Mr. Heape has served as a director of the Company since 1998. He received a B.S. in Geology from Tulane University in 1972. He has engaged in all phases of the oil and gas business since 1972 where he served as an exploration geologist with Lone Star Producing Company, a wholly-owned subsidiary of Lone Star Gas (now TXU, Inc.). From 1972 to 1975, Mr. Heape performed extensive geological work for Lone Star in East Texas, Northern Louisiana, and Southern Arkansas. He joined Bass Enterprises in 1975 and left Bass in 1976 to form H & S Production, Inc., a Texas corporation.

Mr. Heape is a Certified Petroleum Geologist by the American Association of Petroleum Geologists, a Certified Professional Geological Scientist by the Association of Professional Geological Scientists, a member of the Independent Petroleum Association of America (IPAA), the Society of Independent Professional Earth Scientists (SIPES), the Texas Independent Production and Royalty Owners Association (TIPRO), the East Texas Geological Society and the Dallas Geological Society.

Bob G. Honea

Mr. Honea is the President, Treasurer/Secretary, Director (Chief Executive and Financial Officer) and has over 30 years of experience in the domestic and international oil field tubular business. During this time, he has dealt with both major and independent oil and gas companies. Mr. Honea has been an officer and director of the Company since 1998.

Mr. Honea is the President of National Tubular Products, Inc. and NTP Energy, Inc., both of Dallas, Texas.

Benton J. Poole

Mr. Poole received a Bachelor of Business Administration degree from the Texas Tech University in 1973 and a Doctor of Jurisprudence degree from Texas Tech University School of Law in 1976. Mr. Poole has more than 25 years of experience in the private practice of law and is presently a sole practitioner concentrating in oil, gas and mineral law. He is a member of the State Bar of Texas, the American Bar Association and the Dallas Bar Association and is a member of the Oil, Gas and Mineral Law/Energy Law Section of each. Mr. Poole has served as a director of the Company since 1998.

Harvey Jury

Mr. Jury is founder and managing director of Jury & Associates, a Dallas-based management and marketing consulting organization. Jury & Associates and its predecessors have been serving clients throughout the United States since 1970. Jury & Associates clients are active in oil and gas, commercial and residential real estate, title insurance, investment management, banking and trust services, and other financial services.

All officers of the Company hold office until the annual meeting of directors following the annual meeting of stockholders or until their respective successors are duly elected and qualified or their earlier resignation or removal.

Board of Directors and Committee Meetings Attendance

During the fiscal year ended December 31, 2003, the Board acted on seven occasions by written unanimous consent of the Board of Directors in lieu of meeting. The Company has a Compensation Committee which has acted on stock options, but there are no other committees. The full Board functions on other matters.

Section 16(a) of the Exchange Act requires the Company's directors, executive officers and persons who own more than 10 percent of a registered class of the Company's equity securities ("10% holders"), to file with

the Securities and Exchange Commission (the "SEC") initial reports of ownership and reports of changes in ownership of Common Stock and other equity securities of the Company. Directors, officers and 10% holders are required by SEC regulation to furnish the Company with copies of all of the Section 16(a) reports they file.

Based solely on a review of reports furnished to the Company or written representations from the Company's directors and executive officers during the fiscal year ended December 31, 2003, all Section 16(a) filing requirements applicable to its directors, officers and 10% holders for such year were complied with.

#### Code of Ethics

The Board of Directors have discussed the need for a Code of Ethics and have concluded that a Code is not necessary for a company with no employees.

### ITEM 10 - EXECUTIVE COMPENSATION

-----

At March 15, 2004, the Company had no salaried employees, either in field operations or office and administrative activities. The Company contracts with other parties, including officers, directors, principal stockholders or other affiliates of the Company, to perform the office and administrative activities of the Company. The Company also utilizes the services of outside consultants on a contract basis.

As of March 15, 2004 there have been no salaries paid to any of the officers or Directors of the company. Directors have not been compensated in cash for acting in their capacity as Directors. Directors are reimbursed for their accountable expenses incurred in attending meetings and conducting their duties.

### ITEM 11 - SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

-----

The following table sets forth, as of March 15, 2004, information with respect to (1) any person known by the Company to own beneficially more than five percent (5%) of the Company's Common Stock, (2) the shares of Common Stock beneficially owned by each officer and director of the Company, and (3) the total of the Company's Common Stock beneficially owned by the Company's officers and directors as a group. Except as noted in the footnotes, it is the belief of the Company that each stockholder listed below holds the sole voting and investment power with regard to the shares owned beneficially by such stockholder:

<u>Name of Beneficial Owner</u>	<u>Number of Shares Beneficially Owned</u>	<u>Approximate Percent of Common Stock Outstanding<sup>(1)</sup></u>
Scott G. Heape Dallas, Texas <sup>(5)</sup>	2,158,166 <sup>(2)</sup>	12.22
Bob G. Honea Dallas, Texas <sup>(5)</sup>	1,840,000 <sup>(3)</sup>	10.42



Benton J. Poole Dallas, Texas	677,200 <sup>(4)</sup>	3.87
Harvey Jury Dallas, Texas	130,000	0.74
All officers and directors as a group (4 persons)	4,805,366	26.60

- (1) Based upon 17,364,626 shares issued and outstanding as March 14, 2004, after deducting 1,862,000 shares held in the Company's treasury, and including options held by each individual.
- (2) Includes shares owed by H&S Production, Inc. which Mr. Heape owns 100% and shares held by H&S Production, Inc. Pension Trust. Includes options to purchase 300,000 shares which are currently exercisable.
- (3) Includes 820,000 shares held by National Tubular Products, Inc., Profit Sharing Plan & Trust, of which Mr. Honea is the principal beneficiary. Includes options to purchase 300,000 shares which are currently exercisable.
- (4) Includes shares held by Poole & Moffett Profit Sharing Trust fbo Benton J. Poole of which Mr. Poole is the principal beneficiary. Includes options to purchase 100,000 shares which are currently exercisable.
- (5) The address for the beneficial owners is c/o Castleguard Energy, Inc., 4625 Greenville Avenue, Suite 203, Dallas, Texas, 75206.

#### ITEM 12 - CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

-----

In September 2002, the Company entered into a farmout agreement with H & S Production, Inc. related to a proposed well in the Minden Louisiana field. H & S will bear all drilling costs related to the Company's interest and, after payout, will reassign one-half interest to the Company. The Company believes the arrangement adheres to standards in the industry and is as favorable as could have been obtained from an unaffiliated third party.

In October 2003, the Company agreed with H&S Production to rescind the agreement and instead entered into a farmout arrangement with an unrelated party to the extent of a 1/16 interest leaving Castleguard with a .0375 interest in a new well. The third party will reassign to the Company after payout a 20% interest in the 1/16 interest.

The Company rents office space on a month-to-month basis for \$500 per month from Bob Honea, its President.

The Company purchased public relations services during 2003 from its Director Harvey Jury aggregating \$7,200 and reimbursed Mr. Jury's out-of-pocket expenses of \$780.40.

PART IV

ITEM 13 - EXHIBITS AND REPORTS

(a) Exhibits

Item

- 3.1<sup>(1)</sup> Certificate of Incorporation of Castleguard Energy, Inc. incorporated by reference from the 1999 10KSB (Exhibit 3.1).
- 3.2<sup>(2)</sup> Amended and Restated By-Laws of Castleguard Energy, Inc.
- 10.1<sup>(3)</sup> Farmout Agreement between H & S Production, Inc. and the Company dated September 26, 2002
- 10.2 Loan Agreement from Castleguard Energy, Inc as Borrower and First American Bank, SSB in Dallas as Bank dated October 28, 2003
- 31.1 Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 32.1 Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- (1) Previously filed as an exhibit to our 1999 Annual report on Form 10-KSB, and incorporated herein by reference.
- (2) Previously filed as an exhibit to our 2000 Annual report on Form 10-KSB, and incorporated herein by reference.
- (3) Previously filed as an exhibit to Company's Form 8K Report filed with the SEC on October 7, 2002, and incorporated herein by reference.

(b) Reports of Form 8K

None.

ITEM 14 - PRINCIPAL ACCOUNTANT FEES AND SERVICES

-----

The following table sets forth the amount of audit fees, audit-related fees, tax fees and all other fees billed by Whitley Penn for the years ended December 31, 2003 and 2002.

	<u>2003</u>	<u>2002</u>
Audit services (1)	\$ 24,660	\$ 18,025

Edgar Filing: CASTLEGUARD ENERGY INC - Form 10KSB

Audit-related services	-	-
Tax and all other services (2)	<u>2.876</u>	<u>2.500</u>
 Total Fees	 \$ <u>27.536</u>	 \$ <u>20.525</u>

Whitley Penn did not render professional services relating to the financial information systems design and implementation for the years ended December 31, 2003 or 2002.

- (1) Audit services consist of the annual audits of our financial statements included in Form 10-KSB, quarterly reviews of our financial statements included in Form 10-QSB, as well as services related to filings made with the Securities and Exchange Commission and accounting advisory services related to financial accounting matters.
- (2) Tax services include, but are not limited to, assistance with certain tax compliance matters and various tax planning consultations.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

CASTLEGUARD ENERGY, INC.

March 30, 2004

/s/ Bob G. Honea  
 BY: Bob G. Honea, Director/President  
 (Chief Executive and Financial Officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

BOB G. HONEA	Director/President Secretary/Treasurer	
<u>/s/ Bob G. Honea</u>	(Chief Executive and Financial Officer)	March 30, 2004

SCOTT HEAPE		
<u>/s/ Scott Heape</u>	Director	March 30, 2004

BENTON POOLE	Director	March 30, 2004
--------------	----------	----------------

/s/ Benton Poole

HARVEY JURY

/s/ Harvey Jury

Director

March 30, 2004

APPENDIX A

CASTLEGUARD ENERGY, INC.

INDEX TO FINANCIAL INFORMATION

DECEMBER 31, 2003

Financial Review	F-2
Report of Independent Auditors	F-5
Financial Statements:	
Balance Sheets	F-6
Statements of Income	F-7
Statements of Cash Flows	F-8
Statements of Stockholders' Equity	F-9
Notes to Financial Statements	F-10

## Financial Review

The following is a discussion and comparison of the financial condition and results of operations of the Company as of and for the twelve months ended December, 2003 ("2003") compared with the twelve months ended December, 2002 ("2002") and 2002 compared to 2001. This discussion should be read in conjunction with the Company's Financial Statements, the notes related thereto, and the other financial data included elsewhere in this Annual Report on Form 10-KSB.

### Overall Operations

Mechanical difficulties with two of the Minden field wells which started in 2002 continued to adversely affect Castleguard's operations in 2003. The wells were worked over in the fourth quarter of 2002 and resumed production in the first quarter of 2003. Production rates were at significantly lower levels than before and continued to decline throughout the year. As a consequence, production volumes and revenues were both lower than in 2002; cash flows were diminished; financial resources were depleted; and, a significant downward revision in oil and gas reserves at year end 2003 resulted from the decline in production. The reserve reduction in turn caused an increase in the rate of depreciation, depletion and amortization, driving a fourth quarter change in estimates applicable to the full year. The downward revision also triggered a ceiling test impairment writedown of approximately \$203,000 in our investment in oil and gas interests.

### 2003 Results of Operations Compared with 2002

Net loss of (\$122,541) ((\$.01) per share) for 2003 was less than net income of \$105,929 (\$.01 per share) for 2002, primarily from lower volumes in 2003 than in 2002. Revenues declined 27% year over year from declines of 67% in gas volumes and 26% in oil volumes sold, partially offset by increased prices of 110% on gas and 20% on oil. It was also significantly influenced by the impairment writedown of \$203,000 before taxes.

Gas volumes declined sharply in 2003 to 64,412 mcf from 196,507 mcf in 2002 and oil volumes decreased to 3,905 barrels from 5,243 barrels in 2002. Average gas prices in 2003 were \$5.72 per mcf up from \$2.73 per mcf in 2002. Oil prices averaged \$30.14 per barrel in 2003 compared to \$25.04 per barrel in 2002.

Hydrocarbon volumes were adversely impacted by the mechanical difficulties in Minden. Price improvement began in the last half of 2002 and continued higher through year end 2003.

Production costs and taxes trended down in 2003 following the declining production curves. However, the rate of depreciation, depletion and amortization was up sharply in 2003 as a result of the downward revision of reserves reflected in our year-end reserve report.

Administrative costs were essentially unchanged for the year, having reached optimal levels from levels several years ago as the result of continuous cost cutting efforts.

### 2002 Results of Operations Compared with 2001

Net income of \$105,929 (\$.01 per share) for 2002 was less than net income of \$339,716 (\$.02 per share) for 2001, primarily from average natural gas prices 43% lower in 2002 than in 2001. Revenues declined 35% year over year from lower gas prices, a 2% decline in gas volumes sold, modestly offset by an 84% increase in oil sales volumes.

## F-2

Gas volumes declined slightly in 2002 to 196,507 mcf from 201,231 mcf in 2001 and oil volumes increased to 5,243 barrels from 2,848 barrels in 2001. Average gas prices in 2002 were \$2.73 per mcf down from \$4.80 per mcf in 2001. Oil prices averaged \$25.04 per barrel in 2002 compared to \$24.36 per barrel in 2001.

Gas volumes were adversely impacted by mechanical difficulties in Minden during the fourth quarter of 2002 (see separate fourth quarter section) reversing a trend of volume improvement compared to 2001. Prices started the year weak and improved slowly in the last half of 2002, almost the reverse of 2001 which started high and declined throughout the year.

Production costs and taxes trended higher in 2002 reflecting higher oil production and the higher expense of Minden wells in distress prior to being reworked during the fourth quarter. Depreciation, depletion and amortization were at essentially the same rate in 2002 as in 2001.

Administrative costs were reduced 40% from 2001 levels as the result of stringent cost controls employed during a time of weak prices. Interest and financing costs were 64% lower than 2001 as the result of declining debt levels and lower interest rates in 2002. The tax provision for 2002 is at normal rates where the provision for 2001 was reduced by a loss carry-forward which was completely absorbed in 2001.

Reserves

The Company's net proved oil and gas reserves at January 1, 2003 compared with January 1, 2002 plus the changes for those years, as estimated by independent petroleum engineers, are set forth below.

	<u>2003</u>		<u>2002</u>	
	Gas	Oil	Gas	Oil
	<u>(MCF)</u>	<u>(BBL)</u>	<u>(MCF)</u>	<u>(BBL)</u>
Reserves at beginning of year	1,000,096	23,849	1,329,501	10,422
Added by exploration and development	68,116	291	12,549	225
Revisions of previous reserves	(543,065)	(7,306)	(145,447)	18,445
Less production	(64,412)	(3,905)	(196,507)	(5,243)
	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
Reserves at year end	<u>460,735</u>	<u>12,929</u>	<u>1,000,096</u>	<u>23,849</u>

Year 2002 reflects significant additions from revisions to a Minden oil well which was recompleted in mid-2002. No new reserves were added from development activities and the changes to gas reserves were from typical annual revisions to producing wells. Year 2003 reflects the aforementioned downward revisions as a result of rapid decline in Minden production following mechanical problems in 2002.

#### Liquidity and Capital Resources

Early in 2003, we sold our interests in the Mings Chapel Field in Upshur County, Texas. The properties were expensive to operate, production levels were falling below our expectations and we believed that we could redeploy our capital in new projects and reduce debt.

The Louisiana Conservation Commission retroactively reduced the Company's interest in certain sands of a Minden gas well which were productive between 1999 and 2001 requiring us to pay another producer \$83,631 for their share of production which we had received credit for when we acquired our interest in the well. When combined with our share of costs for a well which was drilled but in completion at year end, we were confronted with total capital requirements of more than \$225,000. Recognizing that our resources were limited, we farmed out a portion of the new Minden well to reduce the capital required.

F-3

Farmout notwithstanding, our capital requirements strained our resources and we negotiated a change in our commercial bank agreement to provide more borrowing capacity from which to meet our requirements. All of our available working capital was consumed by year end 2003 and additional amounts were borrowed after year end to meet the requirements. In March 2004, we negotiated a 90 day postponement in principal payments that would have been due pursuant to the loan agreement. We believe the postponement will allow operating cash flow to catch up and provide funds to meet debt obligations.

It should be noted that even though cash flow in 2003 was tight, we were able to reduce our outstanding debt \$246,670 or 62% of the total we owed at the beginning of the year. We expect cash to be tight over the next year and any new opportunities will require finding sources of capital to pursue the opportunities.

#### Fourth Quarter Results

Fourth quarter results in 2003 were adversely impacted by a provision for depreciation, depletion and amortization required by the downward adjustment of reserves and a resulting impairment writedown of approximately \$203,000 related to the Company's investment in oil and gas interests. The provision was the principal cause of a net loss of (\$226,506) compared to a profit of \$8,404 in 2002.

Sales volumes of natural gas were 11,316 MCF in the fourth quarter of 2003 at an average price of \$4.58 versus 15,651 MCF in 2002 at an average price of \$3.73. Oil volumes in the fourth quarter this year were 810 barrels at \$31.74 per barrel versus 1,921 barrels at an average price of \$25.91 in 2002.

F-4

REPORT OF INDEPENDENT AUDITORS

Board of Directors  
Castleguard Energy, Inc.

We have audited the accompanying balance sheets of Castleguard Energy, Inc. as of December 31, 2003 and 2002 and the related statements of income, stockholders' equity and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Castleguard Energy, Inc. as of December 31, 2003 and 2002 and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

/s/ Whitley Penn

Dallas, Texas  
February 13, 2004

F-5

CASTLEGUARD ENERGY INC.  
BALANCE SHEETS

December 31,



Edgar Filing: CASTLEGUARD ENERGY INC - Form 10KSB

	<u>2003</u>	<u>2002</u>
Assets		
Current assets:		
Cash and cash equivalents	\$ 9,501	\$ 126,823
Accounts receivable	<u>2,319</u>	<u>66,719</u>
Total current assets	11,820	193,542
Petroleum and natural gas interests, net	1,191,324	1,476,692
Deferred debt issue costs, net	<u>6,766</u>	<u>18,363</u>
TOTAL ASSETS	\$ <u>1,209,910</u>	\$ <u>1,688,597</u>
Liabilities & Stockholders' Equity		
Current liabilities:		
Accounts payable and accrued liabilities	\$ 74,455	\$ 123,539
Current portion of long-term debt	<u>130,002</u>	<u>260,004</u>
Total current liabilities	204,457	383,543
Long-term debt, less current portion	18,997	135,665
Deferred income taxes	<u>47,042</u>	<u>107,434</u>
TOTAL LIABILITIES	<u>270,496</u>	<u>626,642</u>
Stockholders' equity:		
Common stock, \$0.001 par value, 50,000,000 shares authorized;		
19,226,626 shares issued; 17,364,626 shares outstanding	19,227	19,227
Paid-in capital	965,826	965,826
Retained earnings	<u>10,361</u>	<u>132,902</u>

Edgar Filing: CASTLEGUARD ENERGY INC - Form 10KSB

	995,414	1,117,955
Treasury stock, 1,862,000 shares at cost	<u>(56,000)</u>	<u>(56,000)</u>
	)	)
Total stockholders' equity	<u>939,414</u>	<u>1,061,955</u>
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ <u>1,209,910</u>	\$ <u>1,688,597</u>

See accompanying notes to financial statements.

F-6

CASTLEGUARD ENERGY INC.  
STATEMENTS OF INCOME

	Year Ended December 31,	
	<u>2003</u>	<u>2002</u>
Oil and gas sales	\$ <u>486,894</u>	\$ <u>668,585</u>
Expenses:		
Lease operating expenses and taxes	87,326	131,570
Depreciation, depletion and amortization	206,293	195,578
Impairment of petroleum and natural gas interests	202,969	-
General and administrative	<u>148,732</u>	<u>152,510</u>
	<u>645,320</u>	<u>479,658</u>
Income (loss) from operations	(158,426)	188,927
Interest and financing costs	<u>(24,508)</u>	<u>(37,585)</u>
	)	)
Income (loss) before income taxes	(182,934)	151,342

Provision (benefit) for income taxes	<u>(60,393)</u>	<u>45,413</u>
	)	
Net income (loss)	\$ <u>(122,541)</u>	\$ <u>105,929</u>
Basic and diluted earnings (loss) per common share	\$ <u>(0.01)</u>	\$ <u>0.01</u>
Weighted average number of common shares outstanding	<u>17,364,626</u>	<u>17,334,018</u>

See accompanying notes to financial statements.

F-7

CASTLEGUARD ENERGY INC.  
STATEMENTS OF CASH FLOWS

	Year Ended December 31,	
	<u>2003</u>	<u>2002</u>
Cash Flows from Operating Activities:		
Net income (loss)	\$ (122,541)	\$ 105,929
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation, depletion and amortization	206,293	195,578
Impairment of petroleum and natural gas interests	202,969	
Deferred income taxes	(60,393)	46,434
Amortization of financing costs	11,598	10,632
Issue of common shares for litigation	-	7,396
Change in assets and liabilities:		
Accounts receivable	64,400	80,158
Accounts payable and accrued liabilities	<u>(49,084)</u>	<u>32,344</u>
	)	
Net cash provided by operating activities	<u>253,242</u>	<u>478,471</u>

Cash Flows from Investing Activities:		
Additions to petroleum and natural gas interests	(228,696)	(212,886)
Proceeds from sale of petroleum and natural gas interests	<u>104,802</u>	<u>-</u>
Net cash used in investing activities	<u>(123,894)</u>	<u>(212,886)</u>
	)	)
Cash Flows from Financing Activities:		
Refinancing of bank debt	20,000	583,344
Payments on long-term debt	<u>(266,670)</u>	<u>(822,085)</u>
Net cash used by financing activities	<u>(246,670)</u>	<u>(238,741)</u>
	)	)
Net increase (decrease) in cash and cash equivalents	(117,322)	26,844
Cash and cash equivalents, beginning of year	<u>126,823</u>	<u>99,979</u>
Cash and cash equivalents, end of year	\$ <u>9,501</u>	\$ <u>126,823</u>
Supplemental information:		
Interest paid	\$ <u>11,807</u>	\$ <u>27,235</u>

See accompanying notes to financial statements.

F-8

CASTLEGUARD ENERGY INC.  
 STATEMENTS OF STOCKHOLDERS' EQUITY  
 For the Years Ended December 31, 2003 and 2002

Edgar Filing: CASTLEGUARD ENERGY INC - Form 10KSB

	<u>Common Stock</u>		Paid-in <u>Capital</u>	Treasury <u>Stock</u>	Retained	Total
	<u>Shares</u>	<u>Amount</u>			<u>Earnings</u>	<u>Stockholders'</u>
					<u>(Deficit)</u>	<u>Equity</u>
Balance, December 31, 2001	19,013,626	\$ 19,014	\$ 958,643	\$ (56,000)	\$ 26,973	\$ 948,630
Issuance of shares to settle litigation and other	213,000	213	7,183			7,396
Net income, 2002	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>105,929</u>	<u>105,929</u>
Balance, December 31, 2002	19,226,626	19,227	965,826	(56,000)	132,902	1,061,955
Net loss, 2003	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(122,541)</u>	<u>(122,541)</u>
				)	)	
Balance, December 31, 2003	<u>19,226,626</u>	<u>\$ 19,227</u>	<u>\$ 965,826</u>	<u>\$ (56,000)</u>	<u>\$ 10,361</u>	<u>\$ 939,414</u>

See accompanying notes to financial statements.

F-9

A. Nature of Business

Castleguard Energy, Inc. is an independent energy company engaged in the exploration for and the acquisition, development, exploitation and operation of crude oil and natural gas properties, and in the production of crude oil and natural gas in North America. The Company's activities are conducted principally in the states of Louisiana, Texas and Alabama. The Company's corporate offices are located in Dallas, Texas.

## B. Accounting Policies

A summary of the Company's significant accounting policies consistently applied in the preparation of the accompanying financial statements follows:

### Basis of Accounting

The accounts are maintained and the financial statements have been prepared using the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America.

### Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect certain reported amounts in the financial statements and accompanying notes. Actual results could differ from these estimates and assumptions.

### Cash and Cash Equivalents

The Company considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents. At December 31, 2003 and 2002, the Company had no such investments included in cash and cash equivalents. The Company maintains deposits primarily in one financial institution, which may at times exceed amounts covered by insurance provided by the U.S. Federal Deposit Insurance Corporation ("FDIC").

### Property and Equipment

The Company utilizes the full cost method of accounting for oil and gas properties, which involves capitalizing all acquisitions, exploration and development costs incurred for the purpose of finding oil and gas reserves, including the costs of drilling and equipping productive wells, dry hole costs, lease acquisition costs and delay rentals. The Company also capitalizes the portion of general and administrative costs which can be directly identified with acquisition, exploration or development of oil and gas properties. Costs associated with unevaluated properties are excluded from amortization. Unevaluated property costs are transferred to evaluated property costs at such time as wells are completed on the properties, the properties are sold, or management determines these costs to have been impaired. Cost of properties, including future development, site restoration, dismantlement and abandonment costs, which have proved reserves and those which have been determined to be worthless, are depleted on the unit of production method based on proved reserves. Additionally, the capitalized costs of oil and gas properties cannot exceed the present value of the estimated net cash flow from its proved reserves, together with the lower of cost or estimated fair value of its undeveloped properties (the full cost ceiling). Transactions involving sales of reserves in place, unless extraordinarily large portions of reserves are involved, are recorded as adjustments to accumulated depreciation, depletion and amortization.

F-10

Upon the acquisition or discovery of oil and gas properties, management estimates the future net costs to be incurred to dismantle, abandon and restore the property using geological, engineering and regulatory data available. Such cost estimates are periodically updated for changes in conditions and requirements. Such estimated amounts are considered as part of the full cost pool for purposes of amortization upon acquisition or discovery. Such costs are capitalized as oil and gas properties as the actual restoration, dismantlement and abandonment activities take place.

Office equipment is recorded at cost and depreciated on a straight-line basis over its estimated useful life of two years.

Tangible equipment is recorded at cost and depreciated on a straight-line basis over its estimated useful life of seven years.

#### Income Taxes

Deferred income taxes are determined using the liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates and recognized in income in the period that includes the enactment date. In addition, if necessary, a valuation allowance is established to reduce any deferred tax asset for which it is determined that it is more likely than not that some portion of the deferred tax asset will not be realized.

#### Oil and Gas Sales

Petroleum and natural gas sales are recognized upon delivery to the metered point upstream of the pipeline connection.

#### Earnings per Common Share

Basic earnings per share is calculated by dividing net income available to common stockholders by the weighted average number of common shares outstanding for the period. Diluted earnings per share reflects the potential dilution that could occur if options to issue common stock were exercised or converted into common stock. For the years ended December 31, 2003 and 2002, the Company's potential dilutive options for common shares totaling 1,000,000 shares each year are not included in the dilutive calculation of earnings (loss) per share as the effect would be antidilutive.

#### Stock Options

The Company accounts for its stock options under the recognition and measurement principles of Accounting Principles Board ("APB") Opinion No. 25, *Accounting for Stock Issued to Employees*, and related interpretations. There was no pro forma effect on net income as if the Company had applied the fair value of recognition provisions of SFAS No. 123, *Accounting for Stock-Based Compensation*, to stock-based employee

compensation as of the years ended December 31, 2003 and 2002.

At January 1, 2002 through December 31, 2003, the Company had 1,000,000 stock options outstanding, which were fully vested and exercisable since January 1, 2002, all with an exercise price of \$0.10 per share and a 10 year life, which expire on September 6, 2011.

## F-11

## Fair Value of Financial Instruments

The estimated fair value of accounts receivable, accounts payable and long-term debt approximate their carrying amounts due to the short maturity of their instruments. None of these instruments are held for trading purposes.

## C. Petroleum and Natural Gas Interests

The following table discloses certain financial data relative to the Company's evaluated oil and gas producing activities, which at December 31, 2003 and 2002 are all located in the United States:

	<u>2003</u>	<u>2002</u>
Capitalized Costs incurred during year:		
Exploration costs	\$ 100,295	\$ 104,770
Development costs	<u>128,401</u>	<u>108,116</u>
	\$ <u>228,696</u>	\$ <u>212,886</u>
Petroleum and natural gas interests:		
Balance, beginning of year	\$ 1,939,841	\$ 1,726,955
Additions	228,696	212,886
Sales	<u>(104,802)</u>	<u>-</u>
	)	
Balance, end of year	\$ <u>2,063,735</u>	\$ <u>1,939,841</u>
Accumulated depletion and amortization:		
Balance, beginning of year	\$ 463,149	\$ 267,571
Provision for depletion and amortization	206,293	195,578
Impairment	<u>202,969</u>	<u>-</u>



Balance, end of year	\$ <u>872,411</u>	\$ <u>463,149</u>
Net capitalized costs	\$ <u>1,191,324</u>	\$ <u>1,476,692</u>
Amortization and depletion per mcf	\$ <u>2.35</u>	\$ <u>.86</u>

The foregoing table includes \$83,631 of additions to petroleum and natural gas interests representing amounts paid by the Company to an unrelated party pursuant to a decision by the Louisiana Conservation Commission in which the Commission reduced the Company's interest in certain sands of a Minden, Louisiana well. The decision was retroactive to the date of first production which was prior to acquisition of the Company's interest. Production was substantially before acquisition and reduced the purchase price. Accordingly, the amount refunded was treated as an addition to the purchase price and capitalized.

The table also reflects the provision for impairment writedown of total investment in petroleum and natural gas interests pursuant to a ceiling test calculation that requires such provision when the investment exceeds estimated discounted future cash flow from reserves.

F-12

#### D. Related Party Transactions

In January 2001, the Company entered into an agreement with H & S Production, Inc. (a company wholly owned by the Company's Chairman, Scott Heape) to participate in a farmout agreement covering leasehold interests in the Mings Chapel Field in East Texas whereby the Company had the opportunity to participate in up to three development wells. The first and second wells were drilled, completed, and put on line in 2001. In early 2003, the Company sold for cash its interest in the Mings Chapel properties effective January 1, 2003. No gain or loss was recorded from the sale with credit reducing the Company's net investment in oil and gas properties.

Additionally, in September 2002, the Company entered into a farmout agreement with H & S Production, Inc., related to a proposed well in the Minden Louisiana field. H & S would bear all drilling costs related to the Company's interest and, after payout, would reassign one-half interest to the Company. In October 2003, the Company agreed with H&S Production to rescind the agreement and instead entered into a farmout arrangement with an unrelated party to the extent of a 1/16 interest leaving Castleguard with a 3.75% interest in the new well. The third party will reassign a 20% interest to the Company after payout.

The Company rents office space on a month-to-month basis for \$500 per month from its President. The Company purchased public relations services from a director aggregating \$7,200 for 2003 and reimbursed him \$780.40 for out-of-pocket costs.

#### E. Income Taxes

The Company's provision for income taxes each year is all deferred; no income taxes have been paid during

2002 and 2003. Following is an analysis of the provision (benefit) for income taxes compared to the amounts computed by applying the U.S. federal income tax rate of 34% to pretax income from continuing operations:

	<u>2003</u>	<u>2002</u>
<b>Computed "expected" tax expense (benefit)</b>	<b>\$ (62,198)</b>	<b>\$ 51,456</b>
<b>Increase (decrease) in income tax resulting from:</b>		
<b>Difference in effective rate</b>	<b>1,805</b>	<b>(6,043)</b>
<b>Utilization of net operating loss carryforward</b>	<b><u>-</u></b>	<b><u>-</u></b>
	<b>\$ <u>(60,393)</u></b>	<b>\$ <u>45,413</u></b>

The tax effects of temporary differences that give rise to significant portions of the net deferred tax liabilities at December 31, 2003 and 2002 are presented below:

	<u>2003</u>	<u>2002</u>
<b>Deferred tax liability (asset):</b>		
<b>Difference between financial and tax basis of property</b>	<b>\$ 58,240</b>	<b>\$ 114,071</b>
<b>Net operating loss carryforwards</b>	<b><u>(11,198)</u></b>	<b><u>(6,637)</u></b>
<b>Net deferred tax liability</b>	<b>\$ <u>47,042</u></b>	<b>\$ <u>107,434</u></b>

At December 31, 2003, the Company had net operating loss carryforwards for federal income tax purposes of approximately \$37,000 which were available to offset future federal taxable income, if any, through 2015.

F-13

#### F. Long-Term Debt

In October 2003, the Company entered into a revised debt agreement with a commercial bank. The agreement provides for a \$2,000,000 term note with an initial borrowing base of \$322,333 which is reduced at the rate of \$21,667 per month. Principal payments of \$21,667 per month are due when the amounts outstanding on this note exceed the borrowing base. At December 31, 2003, the borrowing base was \$278,999 and the outstanding note balance was \$148,999. Interest is payable monthly at the bank's prime rate (4.0% at December 31, 2003) plus .75 percent. The note is collateralized by all of the Company's oil and gas properties. Debt covenants restrict other debt, pledge of assets, sales of assets, payment of dividends, mergers and changes in ownership.

Based on the borrowing base and debt balance at December 31, 2003, \$130,002 will be due in 2004 and \$18,997 in 2005.

#### G. Oil and Gas Reserve Information - Unaudited

Edgar Filing: CASTLEGUARD ENERGY INC - Form 10KSB

The Company's net proved oil and gas reserves at December 31, 2003 and 2002 have been estimated by independent petroleum consultants in accordance with guidelines established by the Securities and Exchange Commission. Accordingly, the following reserve estimates are based upon existing economic and operating conditions at the respective year ends.

There are numerous uncertainties inherent in estimating quantities of proved reserves and in providing the future rates of production and timing of development expenditures. The following reserve data represents estimates only and should not be construed as being exact. In addition, the discounted future net cash flows should not be construed as the current market value of the Company's oil and gas properties or the cost that would be incurred to obtain equivalent reserves.

The following table sets forth an analysis of the Company's estimated quantities of proved developed oil and gas reserves (including behind-pipe reserves), all located in the United States (Mcfs represents thousand cubic feet):

	<u>Proved Developed Reserves</u>			
	<u>2003</u>		<u>2002</u>	
	<u>Natural Gas</u> <u>in Mcfs</u>	<u>Oil in</u> <u>Barrels</u>	<u>Natural Gas</u> <u>in Mcfs</u>	<u>Oil in</u> <u>Barrels</u>
Proved producing	158,961	11,920	631,705	23,170
Proved non-producing	<u>301,774</u>	<u>1,009</u>	<u>368,391</u>	<u>679</u>
	<u>460,735</u>	<u>12,929</u>	<u>1,000,096</u>	<u>23,849</u>

Components of change in the foregoing reserves for the last two years are as follows:

	<u>2003</u>		<u>2002</u>	
	<u>Natural Gas</u> <u>in Mcfs</u>	<u>Oil in</u> <u>Barrels</u>	<u>Natural Gas</u> <u>in Mcfs</u>	<u>Oil in</u> <u>Barrels</u>
Reserves at beginning of year	1,000,096	23,849	1,329,501	10,422
Added by exploration and development	68,116	291	12,549	225
Revisions of previous reserves	(543,065)	(7,306)	(145,447)	18,445

\$ 107,434

Edgar Filing: CASTLEGUARD ENERGY INC - Form 10KSB

Less production	<u>(64,412)</u>	<u>(3,905)</u>	<u>(196,507)</u>	<u>(5,243)</u>
	)	)	)	)
Reserves at end of year	<u>460,735</u>	<u>12,929</u>	<u>1,000,096</u>	<u>23,849</u>

F-14

The following table presents the standardized measure of future net cash flows related to proved oil and gas reserves together with changes therein, as defined by the Financial Accounting Standards Board. The oil, condensate and gas price structure utilized to project future net cash flows reflects current prices at December 31, 2003 and 2002, and has been escalated only where known and determinable price changes are provided by contracts and law. Future production and development costs are based on current costs with no escalations. Future net cash flows are the estimated future gross revenue less estimated production and ad valorem taxes, income taxes, operating expenses and capital expenditures. They do not consider business risks, or profit on investment.

	<u>2003</u>	<u>2002</u>
Future cash flows	\$ 2,476,339	\$ 5,268,111
Future production and development costs	(795,573)	(1,256,065)
Income taxes	<u>(188,894)</u>	<u>(1,167,710)</u>
	)	)
Future net cash flows	1,491,872	2,844,336
10% annual discount	<u>(440,753)</u>	<u>(974,990)</u>
	)	)
Standardized measure of discounted future net cash flows	<u>\$ 1,051,119</u>	<u>\$ 1,869,346</u>

The following are principal sources of change in the standardized measure of discounted future net cash flows:

	<u>2003</u>	<u>2002</u>
Standardized measure - beginning of year	\$ 1,869,346	\$ 1,298,847
Increases (decreases):		
Sales and transfers, net of production costs	(399,568)	(537,015)
Net change in sales prices, net of production costs	(407,384)	1,219,134

\$ 107,434

Edgar Filing: CASTLEGUARD ENERGY INC - Form 10KSB

Extensions and discoveries, net of future costs	16,778	22,281
Revisions of quantity estimates	(974,808)	(365,971)
Accretion of discount	274,636	175,913
Net change in income taxes	474,046	(267,894)
Changes in production rates, timing and other	<u>198,073</u>	<u>324,051</u>
Standardized measure - end of year	\$ <u>1,051,119</u>	\$ <u>1,869,346</u>

F-15