

BARNWELL INDUSTRIES INC  
Form 10QSB  
May 16, 2005

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

WASHINGTON, D.C. 20549

**FORM 10-QSB**

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

**For the quarterly period ended March 31, 2005**



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

**Commission File Number 1-5103**

**BARNWELL INDUSTRIES, INC.**

(Exact name of small business issuer as specified in its charter)

**DELAWARE**

(State or other jurisdiction of  
incorporation or organization)

**72-0496921**

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

**1100 Alakea Street, Suite 2900, Honolulu, Hawaii**

**96813**

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(Address of principal executive offices)

(Zip code)

**(808) 531-8400**

(Issuer's telephone number, including area code)

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

As of May 11, 2005 there were 2,723,020 shares of common stock, par value \$0.50, outstanding.

Transitional Small Business Disclosure Format  Yes  No

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**BARNWELL INDUSTRIES, INC.**

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## PART 1. FINANCIAL INFORMATION

Item 1. Financial Statements**BARNWELL INDUSTRIES, INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED BALANCE SHEETS****(Unaudited)**

	March 31, 2005	September 30, 2004
<b><u>ASSETS</u></b>		
<b>CURRENT ASSETS:</b>		
Cash and cash equivalents	\$ 5,787,000	\$ 4,497,000
Certificates of deposit	1,899,000	1,387,000
Accounts receivable, net	6,123,000	5,513,000
Other current assets	3,730,000	2,805,000
<b>TOTAL CURRENT ASSETS</b>	<b>17,539,000</b>	<b>14,202,000</b>
<b>INVESTMENT IN LAND</b>	<b>3,033,000</b>	<b>3,033,000</b>
<b>NET PROPERTY AND EQUIPMENT</b>	<b>55,000,000</b>	<b>47,852,000</b>
<b>TOTAL ASSETS</b>	<b>\$ 75,572,000</b>	<b>\$ 65,087,000</b>
<b><u>LIABILITIES AND STOCKHOLDERS' EQUITY</u></b>		
<b>CURRENT LIABILITIES:</b>		
Accounts payable	\$ 5,891,000	\$ 3,199,000
Accrued liabilities	10,796,000	8,625,000
Income taxes payable		36,000
Other current liabilities	1,045,000	1,011,000
<b>TOTAL CURRENT LIABILITIES</b>	<b>17,732,000</b>	<b>12,871,000</b>
<b>LONG-TERM DEBT</b>	<b>10,307,000</b>	<b>10,165,000</b>
<b>ASSET RETIREMENT OBLIGATION</b>	<b>1,959,000</b>	<b>1,775,000</b>
<b>DEFERRED INCOME TAXES</b>	<b>12,272,000</b>	<b>10,719,000</b>
<b>MINORITY INTEREST</b>	<b>368,000</b>	<b>408,000</b>
<b>STOCKHOLDERS' EQUITY:</b>		
Common stock, par value \$0.50 per share:		
Authorized, 4,000,000 shares; 2,723,020 issued and outstanding at March 31, 2005, 2,664,020 issued and outstanding at September 30, 2004	1,362,000	1,332,000
Additional paid-in capital	2,498,000	2,105,000
Retained earnings	28,192,000	25,543,000
Accumulated other comprehensive income - foreign currency translation adjustments	882,000	169,000
<b>TOTAL STOCKHOLDERS' EQUITY</b>	<b>32,934,000</b>	<b>29,149,000</b>
<b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>	<b>\$ 75,572,000</b>	<b>\$ 65,087,000</b>

See Notes to Condensed Consolidated Financial Statements

## BARNWELL INDUSTRIES, INC.

## AND SUBSIDIARIES

## CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

	Three months ended March 31,		Six months ended March 31,	
	2005	2004	2005	2004
<b>Revenues:</b>				
Oil and natural gas	\$ 7,189,000	\$ 5,680,000	\$ 14,657,000	\$ 10,720,000
Sale of interest in leasehold land, net	150,000	7,030,000	300,000	7,030,000
Sale of development rights, net			2,497,000	2,497,000
Contract drilling	2,272,000	730,000	4,377,000	1,030,000
Gas processing and other	212,000	480,000	399,000	853,000
	<b>9,823,000</b>	<b>13,920,000</b>	<b>22,230,000</b>	<b>22,130,000</b>
<b>Costs and expenses:</b>				
Oil and natural gas operating	1,287,000	1,409,000	2,747,000	2,731,000
Contract drilling operating	1,531,000	701,000	3,028,000	1,036,000
General and administrative	3,043,000	3,032,000	5,870,000	5,028,000
Depreciation, depletion and amortization	2,098,000	1,674,000	4,301,000	3,218,000
Interest expense	149,000	157,000	289,000	290,000
Minority interest in earnings (losses)	(40,000)	1,742,000	473,000	2,259,000
	<b>8,068,000</b>	<b>8,715,000</b>	<b>16,708,000</b>	<b>14,562,000</b>
<b>Earnings before income taxes</b>	<b>1,755,000</b>	<b>5,205,000</b>	<b>5,522,000</b>	<b>7,568,000</b>
<b>Income tax provision</b>	<b>845,000</b>	<b>1,465,000</b>	<b>2,172,000</b>	<b>918,000</b>
<b>NET EARNINGS</b>	<b>\$ 910,000</b>	<b>\$ 3,740,000</b>	<b>\$ 3,350,000</b>	<b>\$ 6,650,000</b>
<b>BASIC EARNINGS PER COMMON SHARE</b>	<b>\$ 0.33</b>	<b>\$ 1.42</b>	<b>\$ 1.24</b>	<b>\$ 2.52</b>
<b>DILUTED EARNINGS PER COMMON SHARE</b>	<b>\$ 0.32</b>	<b>\$ 1.33</b>	<b>\$ 1.17</b>	<b>\$ 2.38</b>
<b>Weighted average common shares outstanding:</b>				
Basic	2,722,798	2,642,734	2,711,971	2,635,840
Diluted	2,875,567	2,813,752	2,860,017	2,788,450

See Notes to Condensed Consolidated Financial Statements



**BARNWELL INDUSTRIES, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(Unaudited)

	Six months ended March 31,	
	2005	2004
Cash flows from operating activities:		
Net earnings	\$ 3,350,000	\$ 6,650,000
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation, depletion, and amortization	4,301,000	3,218,000
Minority interest in earnings	473,000	2,259,000
Accretion of asset retirement obligation	58,000	38,000
Gain on sale of contract drilling yard		(139,000)
Deferred income taxes	(315,000)	(820,000)
Sale of development rights, net	(2,497,000)	(2,497,000)
Sale of interest in leasehold land, net	(300,000)	(7,030,000)
	5,070,000	1,679,000
Increase (decrease) from changes in current assets and liabilities	3,731,000	(961,000)
Net cash provided by operating activities	8,801,000	718,000
Cash flows from investing activities:		
Proceeds from matured certificates of deposit	1,288,000	
Proceeds from sale of development rights, net	2,497,000	2,497,000
Proceeds from sale of interest in leasehold land, net	300,000	10,505,000
Proceeds from collection of note receivable		1,311,000
Proceeds from sale of contract drilling yard, net		440,000
Investments in certificates of deposit	(1,800,000)	(1,285,000)
Capital expenditures	(9,087,000)	(4,855,000)
Net cash (used in) provided by investing activities	(6,802,000)	8,613,000
Cash flows from financing activities:		
Distributions to minority interest partners	(513,000)	(2,633,000)
Repayments of long-term debt, net		(1,293,000)
Payment of dividends	(475,000)	(923,000)
Proceeds from exercise of stock options	197,000	178,000
Net cash used in financing activities	(791,000)	(4,671,000)
Effect of exchange rate changes on cash and cash equivalents	82,000	4,000
Net increase in cash and cash equivalents	1,290,000	4,664,000
Cash and cash equivalents at beginning of period	4,497,000	1,648,000
Cash and cash equivalents at end of period	\$ 5,787,000	\$ 6,312,000
Supplemental disclosures of cash flow information:		
Cash paid during the period for:		
Interest	\$ 268,000	\$ 269,000
Income taxes	\$ 2,377,000	\$ 2,228,000

Supplemental disclosure of non-cash investing and financing activities:

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In October 2004, 36,362 stock options (split-adjusted) were exercised in exchange for 10,000 shares (split-adjusted) of Barnwell stock at a market price of \$23.75 per share (split-adjusted), resulting in a \$9,000 increase in common stock, a \$228,000 increase in additional paid-in capital, and a \$237,000 increase in treasury stock.

In December 2003, Barnwell purchased the premises and associated fee simple land interest of its corporate office in Honolulu, Hawaii, for \$1,057,000, of which \$883,000 was financed by long-term debt; the debt was subsequently repaid in full in June 2004.

See Notes to Condensed Consolidated Financial Statements

## BARNWELL INDUSTRIES, INC. AND SUBSIDIARIES

## CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY AND COMPREHENSIVE INCOME

Three months ended March 31, 2005 and 2004

(Unaudited)

	Common Stock	Additional Paid-In Capital	Comprehensive Income	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Total Stockholders Equity
At December 31, 2003 as previously reported	\$ 821,000	\$ 3,139,000		\$ 24,665,000	\$ (682,000)	\$ (4,854,000)	\$ 23,089,000
100% stock dividend to effect a 2-for-1 stock split	494,000	(1,285,000)		(4,063,000)		4,854,000	
Exercise of stock options, 29,000 shares (split-adjusted)	14,000	164,000					178,000
Dividends declared (\$0.25 per share, split-adjusted)				(660,000)			(660,000)
Comprehensive income:							
Net earnings			\$ 3,740,000	3,740,000			3,740,000
Other comprehensive loss, net of income taxes foreign currency translation adjustments			(246,000)		(246,000)		(246,000)
Total comprehensive income			\$ 3,494,000				
At March 31, 2004	\$ 1,329,000	\$ 2,018,000		\$ 23,682,000	\$ (928,000)		\$ 26,101,000
At December 31, 2004	\$ 1,357,000	\$ 2,444,000		\$ 27,418,000	\$ 1,603,000		\$ 32,822,000
Exercise of stock options, 10,000 shares (split-adjusted)	5,000	54,000					59,000
Dividends declared (\$0.05 per share, split-adjusted)				(136,000)			(136,000)
Comprehensive income:							
Net earnings			\$ 910,000	910,000			910,000
Other comprehensive loss, net of income taxes foreign currency translation adjustments			(721,000)		(721,000)		(721,000)
Total comprehensive income			\$ 189,000				
At March 31, 2005	\$ 1,362,000	\$ 2,498,000		\$ 28,192,000	\$ 882,000		\$ 32,934,000

See Notes to Condensed Consolidated Financial Statements



## BARNWELL INDUSTRIES, INC. AND SUBSIDIARIES

## CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY AND COMPREHENSIVE INCOME

Six months ended March 31, 2005 and 2004

(Unaudited)

	Common Stock	Additional Paid-In Capital	Comprehensive Income	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Total Stockholders Equity
At September 30, 2003 as previously reported \$	821,000	\$ 3,139,000		\$ 22,018,000	\$ (1,491,000)	\$ (4,854,000)	\$ 19,633,000
100% stock dividend to effect a 2-for-1 stock split	494,000	(1,285,000)		(4,063,000)		4,854,000	
Exercise of stock options, 29,000 shares (split-adjusted)	14,000	164,000					178,000
Dividends declared (\$0.35 per share, split-adjusted)				(923,000)			(923,000)
Comprehensive income:							
Net earnings			\$ 6,650,000	6,650,000			6,650,000
Other comprehensive income, net of income taxes foreign currency translation adjustments			563,000		563,000		563,000
Total comprehensive income			\$ 7,213,000				
At March 31, 2004	\$ 1,329,000	\$ 2,018,000		\$ 23,682,000	\$ (928,000)		\$ 26,101,000
At September 30, 2004 as previously reported \$	830,000	\$ 3,399,000		\$ 29,605,000	\$ 169,000	\$ (4,854,000)	\$ 29,149,000
100% stock dividend to effect a 2-for-1 stock split	512,000	(1,315,000)		(4,288,000)		5,091,000	
Exercise of stock options, 59,000 shares (split-adjusted) net of 10,000 shares (split-adjusted) tendered and placed in treasury	20,000	414,000				(237,000)	197,000
Dividends declared (\$0.175 per share, split-adjusted)				(475,000)			(475,000)
Comprehensive income:							
Net earnings			\$ 3,350,000	3,350,000			3,350,000

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Other comprehensive income, net of income taxes foreign currency translation adjustments		713,000		713,000		713,000
<b>Total comprehensive income</b>		<b>\$ 4,063,000</b>				

<b>At March 31, 2005</b>	<b>\$ 1,362,000</b>	<b>\$ 2,498,000</b>	<b>\$ 28,192,000</b>	<b>\$ 882,000</b>	<b>\$ 32,934,000</b>
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See Notes to Condensed Consolidated Financial Statements

**BARNWELL INDUSTRIES, INC.**

**AND SUBSIDIARIES**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(Unaudited)**

**1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

The Condensed Consolidated Balance Sheet as of March 31, 2005, the Condensed Consolidated Statements of Operations for the three and six months ended March 31, 2005 and 2004, the Condensed Consolidated Statements of Cash Flows for the six months ended March 31, 2005 and 2004, and the Condensed Consolidated Statements of Stockholders' Equity and Comprehensive Income for the three and six months ended March 31, 2005 and 2004 have been prepared by Barnwell Industries, Inc. (referred to herein together with its subsidiaries as "Barnwell") and are unaudited. In the opinion of management, all adjustments (which include only normal recurring adjustments) necessary to present fairly the financial position, results of operations and cash flows at March 31, 2005 and for all periods presented have been made. The Condensed Consolidated Balance Sheet as of September 30, 2004 has been derived from audited financial statements and adjusted for a common stock split (see Note 2).

Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted. It is suggested that these condensed consolidated financial statements be read in conjunction with the financial statements and notes thereto included in Barnwell's September 30, 2004 annual report on Form 10-KSB. The results of operations for the period ended March 31, 2005 are not necessarily indicative of the operating results for the full year.

The preparation of the financial statements in conformity with accounting principles generally accepted in the United States of America requires management of Barnwell to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses and the disclosure of contingent assets and liabilities. Actual results could differ significantly from those estimates.

**2. COMMON STOCK SPLIT**

*In December 2004, Barnwell's Board of Directors declared a two-for-one stock split in the form of a 100% stock dividend. The shares were distributed on January 28, 2005 to all shareholders of record as of January 11, 2005. There were 1,361,510 shares outstanding on January 11, 2005. Barnwell issued 1,028,223 of new shares and utilized 333,287 shares of treasury stock to execute the stock dividend. Barnwell's common stock began trading on a split-adjusted basis on January 31, 2005. All affected stockholders' equity accounts and shares outstanding, earnings per share and stock option information in this Form 10-QSB have been adjusted to reflect the stock split for all periods presented.*

3. **EARNINGS PER COMMON SHARE**

Basic earnings per share ( EPS ) is computed by dividing net earnings by the weighted-average number of common shares outstanding for the period. The weighted-average number of common shares



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outstanding (split-adjusted) was 2,722,798 and 2,711,971 for the three and six months ended March 31, 2005, respectively, and 2,642,734 and 2,635,840 for the three and six months ended March 31, 2004, respectively.

Diluted EPS includes the potentially dilutive effect of outstanding common stock options using the treasury stock method. The weighted-average number of common and potentially dilutive common shares outstanding (split-adjusted) were 2,875,567 and 2,860,017 for the three and six months ended March 31, 2005, respectively, and 2,813,752 and 2,788,450 for the three and six months ended March 31, 2004, respectively.

Reconciliations between the numerator and denominator of the basic and diluted earnings per share (split-adjusted) computations for the three and six months ended March 31, 2005 and 2004 are as follows:

	Three months ended March 31, 2005		
	Net Earnings (Numerator)	Shares (Denominator)	Per-Share Amount
Basic earnings per share	\$ 910,000	2,722,798	\$ 0.33
Effect of dilutive securities - common stock options		152,769	
Diluted earnings per share	\$ 910,000	2,875,567	\$ 0.32

	Six months ended March 31, 2005		
	Net Earnings (Numerator)	Shares (Denominator)	Per-Share Amount
Basic earnings per share	\$ 3,350,000	2,711,971	\$ 1.24
Effect of dilutive securities - common stock options		148,046	
Diluted earnings per share	\$ 3,350,000	2,860,017	\$ 1.17

	Three months ended March 31, 2004		
	Net Earnings (Numerator)	Shares (Denominator)	Per-Share Amount
Basic earnings per share	\$ 3,740,000	2,642,734	\$ 1.42
Effect of dilutive securities - common stock options		171,018	
Diluted earnings per share	\$ 3,740,000	2,813,752	\$ 1.33

	Six months ended March 31, 2004		
	Net Earnings (Numerator)	Shares (Denominator)	Per-Share Amount
Basic earnings per share	\$ 6,650,000	2,635,840	\$ 2.52
Effect of dilutive securities - common stock options		152,610	
Diluted earnings per share	\$ 6,650,000	2,788,450	\$ 2.38

**4. CASH AND CASH EQUIVALENTS AND CERTIFICATES OF DEPOSIT**

Cash and cash equivalents include cash on hand, demand deposits and short-term investments with original maturities of three months or less. Certificates of deposit at March 31, 2005 and September 30, 2004 include certificates of deposit at various financial institutions with original maturities in excess of three months and are excluded from cash and cash equivalents and are reported separately on the Condensed Consolidated Balance Sheets.

**5. INVESTMENT IN LAND**

Barnwell owns a 77.6% controlling interest in Kaupulehu Developments, a Hawaii general partnership which owns interests in leasehold land and development rights for property located approximately six miles north of the Kona International Airport in the North Kona District of the Island of Hawaii, adjacent to and north of the Four Seasons Resort Hualalai at Historic Kaupulehu, between the Queen Kaahumanu Highway and the Pacific Ocean.

The development rights held by Kaupulehu Developments are for residentially zoned leasehold land within and adjacent to the Hualalai Golf Club and are under option to Kaupulehu Makai Venture, an unrelated entity that is an affiliate of Kajima Corporation of Japan. In December 2004, Kaupulehu Makai Venture exercised the portion of its development rights option that was to expire on December 31, 2004 and paid Kaupulehu Developments \$2,656,000. Revenue from the development rights sale was reduced by \$159,000 of fees related to the sale. All capitalized costs associated with Kaupulehu Developments' development rights were expensed in previous years as Barnwell accounts for sales of development rights under option by use of the cost recovery method, therefore there were no other expenses related to the sale. The \$2,497,000 of option revenue, net of fees, is recorded in the Condensed Consolidated Statements of Operations for the six months ended March 31, 2005 as Sale of development rights, net. There were no sales of development rights in the three months ended March 31, 2005. The December 2004 option receipt represents the fourth of ten scheduled annual option payments. The next scheduled development rights option payment is due on or before December 31, 2005. The total amount of remaining future option receipts, if all options are fully exercised, is \$15,937,500 as of the date of this filing, comprised of six payments of \$2,656,250 due on each December 31 of years 2005 to 2010. If any annual option payment is not made, the then remaining development right options will expire. There is no assurance that any portion of the remaining options will be exercised.

*The aforementioned \$159,000 in fees (\$112,000, net of minority interest) on the \$2,656,000 development rights proceeds were paid in January 2005 to Nearco, Inc., a company controlled by Mr. Terry Johnston, a director of Barnwell and an indirect 21.8% owner of Kaupulehu Developments. Under an agreement entered into in 1987, prior to Mr. Johnston's election to Barnwell's Board of Directors, Barnwell is obligated to pay Nearco 2% of certain Kaupulehu Developments' gross receipts from the sale of real estate interests. In addition, Cambridge Hawaii Limited Partnership, a 49.9% partner of Kaupulehu Developments, in which Barnwell purchased a 55.2% interest in April 2001, is obligated under an agreement entered into in 1987 to pay Nearco 4% of certain Kaupulehu Developments' gross receipts from the sale of real estate interests. The fees represent compensation for promotion and marketing of Kaupulehu Developments' property and were determined based on the estimated fair value of such services. Barnwell believes the fees are fair and reasonable compensation for such services.*

*In February 2004, Kaupulehu Developments entered into a Purchase and Sale Agreement with WB KD Acquisition, LLC ( WB ) by which Kaupulehu Developments transferred its leasehold interest in approximately 870 acres zoned for resort/residential development, in two increments, to WB. There is no affiliation between Kaupulehu Developments and WB. WB is an affiliate of Westbrook Partners, developers of the Kuki o Resort. The first increment ( Increment I ) is an area planned for approximately 80 single-family lots and a beach club on the portion of the property bordering the Pacific Ocean. The purchasers of the 80 single-family lots will have the right to apply for membership in the Kuki o Resort Golf and Beach Club, which is located adjacent to and south of the Four Seasons Resort Hualalai at Historic Ka upulehu. The second increment ( Increment II ) is the remaining portion of the approximately 870-acre property and is zoned for single-family and multi-family residential units and a golf course and clubhouse.*

*With respect to Increment I, Kaupulehu Developments received a non-refundable \$11,550,000 payment ( Closing Payment ) in February 2004 and is entitled to receive payment of the following percentages of the gross proceeds generated from the sale by WB of all single-family lots in Increment I ( Percentage Payments ): 9% of the gross proceeds from single-family lot sales up to aggregate gross proceeds of \$100,000,000; 10% of such aggregate gross proceeds greater than \$100,000,000 but less than \$300,000,000; and 14% of such aggregate gross proceeds in excess of \$300,000,000. If prior to December 31, 2005, Kaupulehu Developments has not received percentage payments equal to or greater than \$2,500,000 in the aggregate, WB will pay Kaupulehu Developments the amount by which the aggregate amount of all prior Percentage Payments made by WB to Kaupulehu Developments is less than \$2,500,000. If prior to December 31, 2006, Kaupulehu Developments has not received Percentage Payments (including payments in lieu of Percentage Payments as described in the immediately preceding sentence) equal to or greater than \$5,000,000 in the aggregate, then WB will pay Kaupulehu Developments the amount by which the aggregate amount of all such payments is less than \$5,000,000. Additionally, WB agreed to pay Kaupulehu Developments non-refundable interim payments of \$50,000 per month ( Interim Payments ), until the first to occur of the closing of the sale of the 40th single-family lot sold in Increment I or WB s payment to Kaupulehu Developments of a total of \$900,000 in Interim Payments subsequent to February 2004. As of March 31, 2005, Kaupulehu Developments has received a total of \$650,000 of Interim Payments subsequent to February 2004. There is no assurance that any future Interim Payments or any Percentage Payments will be received.*

*During the three and six months ended March 31, 2005, Kaupulehu Developments received \$150,000 and \$300,000 of Increment I interim payments, respectively. These payments are reflected in the Condensed Consolidated Statements of Operations for the three and six months ended March 31, 2005 as Sale of interest in leasehold land, net.*

*Kaupulehu Developments, WB and The Trustees of The Estate of Bernice Pauahi Bishop ( KS ) also entered into an agreement (the Step-In Rights Agreement ) whereby if WB elects not to proceed with development of Increment I within the time frame set forth in the Step-In Rights Agreement, which may be extended by KS, or defaults under the terms of its lease with KS, Kaupulehu Developments would have the right to succeed to WB s development rights and develop the property without any payment to WB.*

*In March 2004, WB commenced engineering of infrastructure, preparation of covenants, conditions and restrictions for a community association, and preparation of legal documents to enable real estate sales, and broke ground and graded several miles of access roads. In late September 2004,*

*WB began mass grading of the first phase of 38 lots for development. In late December 2004, WB received final subdivision approval from the County of Hawaii for this first phase of 38 lots.*

*For Increment II, Kaupulehu Developments and WB agreed to use diligent efforts to negotiate, and attempt to document and enter into, prior to the date which is three (3) years following the closing of the sale of the first single-family lot in Increment I, an agreement with regards to the ownership and development of Increment II. WB, however, may terminate such negotiations at any time without any further obligation. Under the terms of the Step-In Rights Agreement, if at the end of three years following the closing of the sale of the first single-family lot in Increment I the parties have not entered into a definitive agreement with respect to Increment II, the leasehold rights with respect to Increment II will revert to Kaupulehu Developments.*

*The interests held by Kaupulehu Developments at March 31, 2005 include the development rights under option; the rights to receive percentage and interim payments from the February 2004 sale of its interest in leasehold land; the leasehold land zoned for resort/residential development within Increment II, which is under a right of negotiation with WB; and approximately 1,000 acres of vacant leasehold land zoned conservation. These interests relate to land located adjacent to and north of the Four Seasons Resort Hualalai at Historic Kaupulehu, between the Queen Kaahumanu Highway and the Pacific Ocean.*

**6. SEGMENT INFORMATION**

Barnwell operates three segments: exploring for, developing, producing and selling oil and natural gas (oil and natural gas); investing in leasehold land in Hawaii (land investment); and drilling wells and installing and repairing water pumping systems in Hawaii (contract drilling). Barnwell's reportable segments are strategic business units that offer different products and services. They are managed separately as each segment requires different operational methods, operational assets and marketing strategies.

Barnwell does not allocate general and administrative expenses, interest expense, interest income or income taxes to segments, and there are no transactions between segments that affect segment profit or loss.

	Three months ended March 31,		Six months ended March 31,	
	2005	2004	2005	2004
<b>Revenues:</b>				
Oil and natural gas	\$ 7,189,000	\$ 5,895,000	\$ 14,657,000	\$ 11,103,000
Land investment	150,000	7,130,000	2,797,000	9,777,000
Contract drilling	2,272,000	730,000	4,377,000	1,030,000
Other	181,000	142,000	345,000	155,000
Total before interest income	9,792,000	13,897,000	22,176,000	22,065,000
Interest income	31,000	23,000	54,000	65,000
Total revenues	\$ 9,823,000	\$ 13,920,000	\$ 22,230,000	\$ 22,130,000
<b>Depreciation, depletion and amortization:</b>				
Oil and natural gas	\$ 2,020,000	\$ 1,589,000	\$ 4,146,000	\$ 3,044,000
Contract drilling	23,000	24,000	47,000	49,000
Other	55,000	61,000	108,000	125,000
Total	\$ 2,098,000	\$ 1,674,000	\$ 4,301,000	\$ 3,218,000
<b>Operating profit (loss) (before general and administrative expenses):</b>				
Oil and natural gas	\$ 3,882,000	\$ 2,897,000	\$ 7,764,000	\$ 5,328,000
Land investment, net of minority interest	116,000	5,312,000	2,184,000	7,380,000
Contract drilling	718,000	5,000	1,302,000	(55,000)
Other	126,000	81,000	237,000	30,000
Total	4,842,000	8,295,000	11,487,000	12,683,000
<b>General and administrative expenses, net of minority interest</b>				
	(2,969,000)	(2,956,000)	(5,730,000)	(4,890,000)
Interest expense	(149,000)	(157,000)	(289,000)	(290,000)
Interest income	31,000	23,000	54,000	65,000
Earnings before income taxes	\$ 1,755,000	\$ 5,205,000	\$ 5,522,000	\$ 7,568,000

## 7. INCOME TAXES

The current and deferred components of the provision for income taxes for the three and six months ended March 31, 2005 and 2004 are as follows:

	Three months ended March 31,		Six months ended March 31,	
	2005	2004	2005	2004
Current	\$ 966,000	\$ 1,050,000	\$ 2,487,000	\$ 1,738,000
Deferred	(121,000)	415,000	(315,000)	(820,000)
	\$ 845,000	\$ 1,465,000	\$ 2,172,000	\$ 918,000

In November 2003, Royal Assent was received on a bill passed by the Parliament of Canada, which was then enacted into law, to reduce Canada's corporate tax rate on resource income (income derived from oil and natural gas operations) over a four-year period beginning January 1, 2003 from 29% to 21% with the 21% tax rate commencing on January 1, 2007. Additionally, the bill phases in over the same four-year period tax deductions for royalties, which previously were not tax deductible, and phases out the Resource Allowance deduction along with other changes. Accordingly, during the six months ended March 31, 2004, Barnwell's Canadian deferred income tax liabilities were reduced by approximately \$1,440,000 due to the reduction in Canada's corporate tax rate. There was no benefit attributable to changes in Canada's corporate tax rate on resource income in the three months ended March 31, 2004 or three and six months ended March 31, 2005.

Barnwell's Canadian deferred income tax liabilities were also reduced in the six months ended March 31, 2004 as a result of the Province of Alberta's reduction of the province's corporate tax rate from 13.0% to 12.5%, effective April 1, 2003. The bill was enacted into law in December 2003. The reduction in the tax rate reduced Canadian deferred income taxes liabilities by approximately \$100,000 in the six months ended March 31, 2004. There were no such changes enacted into law in the three months ended March 31, 2004 or three and six months ended March 31, 2005.

## 8. PENSION PLAN

The following table details the components of net periodic benefit cost for the three and six months ended March 31, 2005 and 2004:

	Three months ended March 31,		Six months ended March 31,	
	2005	2004	2005	2004
Service cost	\$ 34,000	\$ 38,000	\$ 68,000	\$ 76,000
Interest cost	48,000	46,000	96,000	91,000
Expected return on plan assets	(41,000)	(39,000)	(82,000)	(78,000)
Amortization of prior service cost	2,000	1,000	3,000	3,000
Amortization of net actuarial loss	6,000	5,000	12,000	9,000
Net periodic benefit cost	\$ 49,000	\$ 51,000	\$ 97,000	\$ 101,000

Barnwell contributed \$150,000 to the plan during the three and six months ended March 31, 2005. Barnwell estimates that it will contribute between \$0 and approximately \$50,000 to the plan during the remainder of fiscal 2005.

## 9. STOCK-BASED COMPENSATION

Barnwell applies the provisions of Accounting Principles Board Opinion No. 25 in accounting for stock-based compensation and adopted the disclosure-only provisions of Statement of Financial Accounting Standards No. 123, Accounting for Stock-Based Compensation. Had compensation cost for stock options granted since October 1, 1995 been determined based on the fair value method of measuring stock-based compensation provisions of Statement of Financial Accounting Standards No. 123, Barnwell's net earnings and basic and diluted earnings per share (split-adjusted) would have been as follows:

	Three months ended March 31,		Six months ended March 31,	
	2005	2004	2005	2004
Net earnings, as reported	\$ 910,000	\$ 3,740,000	\$ 3,350,000	\$ 6,650,000
Add: Stock-based employee compensation expense included in reported net earnings, net of related tax effects	825,000	346,000	1,459,000	550,000
Deduct: Total stock based employee compensation expense determined under the fair value based method for all awards, net of related tax effects	(864,000)	(346,000)	(1,510,000)	(550,000)
Pro forma net earnings	\$ 871,000	\$ 3,740,000	\$ 3,299,000	\$ 6,650,000
Basic Earnings Per Share:				
As reported	\$ 0.33	\$ 1.42	\$ 1.24	\$ 2.52
Pro forma	\$ 0.32	\$ 1.42	\$ 1.22	\$ 2.52
Diluted Earnings Per Share:				
As reported	\$ 0.32	\$ 1.33	\$ 1.17	\$ 2.38
Pro forma	\$ 0.30	\$ 1.33	\$ 1.15	\$ 2.38

During the three and six months ended March 31, 2005, Barnwell issued 10,000 and 69,000 shares (split-adjusted), respectively, of its common stock to certain employees resulting from exercises of previously granted qualified stock options.

In December 2004, Barnwell granted qualified stock options to certain officers/directors of Barnwell to acquire 70,000 shares (split-adjusted) of Barnwell's common stock at a weighted average exercise price per share of \$27.70 (split-adjusted). These options vest annually over four years

commencing one year from the date of grant and expire in December 2014 and December 2009. No compensation cost was recognized for options granted under this plan for the three and six months ended March 31, 2005 and 2004. At March 31, 2005, 2,000 shares (split-adjusted) were available for grant under the qualified option plan.

In December 2004, Barnwell granted stock options to certain officers/directors of Barnwell to acquire 70,000 shares (split-adjusted) of Barnwell's common stock under a non-qualified plan at a purchase price of \$26.40 per share (market price on date of grant, split-adjusted), with 14,000 of such options vesting annually commencing one year from the date of grant. These options have stock appreciation rights that permit the holder to receive stock, cash or a combination thereof equal to the amount by which the fair market value, at the time of exercise of the option, exceeds the option price. The options expire in December 2014. Barnwell recognized \$256,000 and \$284,000 of compensation costs relating to these options in the three and six months ended March 31, 2005, respectively.

In prior years, Barnwell granted stock options under a non-qualified plan with stock appreciation rights that permit the holder to receive stock, cash or a combination thereof equal to the amount by which the fair market value, at the time of exercise of the option, exceeds the option price. During the three and six months ended March 31, 2005, a portion of the stock appreciation rights were exercised, and the difference between the exercise price and the market price was paid in cash. Barnwell recognized compensation costs of \$1,037,000 and \$2,003,000 in the three and six months ended March 31, 2005, respectively, and compensation costs of \$542,000 and \$861,000 in the three and six months ended March 31, 2004, respectively, relating to these options. There were no exercises of non-qualified stock options in the three and six months ended March 31, 2004.

Stock options at March 31, 2005 were as follows:

Range of exercise prices	Number of Shares	Options outstanding		Options exercisable	
		Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Number of Shares	Weighted Average Exercise Price
\$5.9375 - \$7.8125	142,000	4.0 years	\$ 6.73	142,000	\$ 6.73
\$25.8500 - \$28.4350	140,000	7.9 years	\$ 27.05		
\$5.9375 - \$28.4350	282,000	6.0 years	\$ 16.82	142,000	\$ 6.73

#### 10. RECENT ACCOUNTING PRONOUNCEMENTS

In November 2004, the Financial Accounting Standards Board ( FASB ) issued Statement of Financial Accounting Standards ( SFAS ) No. 151, Inventory Costs, an amendment of Accounting Research Bulletin ( ARB ) No. 43, Chapter 4. SFAS No. 151 amends the guidance in ARB No. 43, Chapter 4, Inventory Pricing to clarify the accounting for abnormal amounts of idle facility expense, freight handling costs, and wasted material (spoilage). SFAS No. 151 requires that those items be recognized as current-period charges regardless of whether they meet the criterion of so abnormal. In addition, SFAS No. 151 requires that allocation of fixed production overhead to the costs of conversion be based on the normal capacity of the production facilities. The provisions of SFAS No. 151 will be



effective for fiscal years beginning after June 15, 2005. Adoption of the provisions of SFAS No. 151 is not expected to have a material impact on Barnwell's financial condition, results of operations, or liquidity.

In December 2004, the FASB issued SFAS No. 123(R), Share-Based Payment. SFAS No. 123(R) replaces SFAS No. 123, Accounting for Stock Issued to Employees, and supersedes Accounting Principles and Standards (APB) Opinion No. 25, Accounting for Stock Issued to Employees. SFAS No. 123(R) requires that compensation costs relating to share-based payment transactions be recognized in the consolidated financial statements. Compensation costs will be measured based on the fair value of the equity or liability instruments issued. SFAS No. 123(R) is effective, as adjusted by the U.S. Securities and Exchange Commission, as of the beginning of the first annual reporting period that begins after June 15, 2005, or for small business filers, as of the beginning of the first annual reporting period that begins after December 15, 2005. Barnwell is currently evaluating the provisions of SFAS No. 123(R) and has not yet determined whether it will use the modified prospective or the modified retrospective methods allowed by SFAS No. 123(R), nor has it determined its impact on its financial condition, results of operations, or liquidity.

In December 2004, the FASB issued SFAS No. 152, Accounting for Real Estate Time-Sharing Transactions, an amendment of FASB Statements No. 66 and 67. SFAS No. 152 amends SFAS No. 66, Accounting for Sales of Real Estate, to reference the financial accounting and reporting guidance for real estate time-sharing transactions provided in AICPA Statement of Position (SOP) 04-2, Accounting for Real Estate Time-Sharing Transactions. SFAS No. 152 also amends SFAS No. 67, Accounting for Costs and Initial Rental Operations of Real Estate Projects, to state that the guidance for incidental operations and costs incurred to sell real estate projects does not apply to real estate time-sharing transactions. The accounting for such operations and costs is subject to the guidance in SOP 04-2. SFAS No. 152 is effective for financial statements for fiscal years beginning after June 15, 2005, with earlier application encouraged. Adoption of the provisions of SFAS No. 152 is not expected to have a material impact on Barnwell's financial condition, results of operations, or liquidity.

In December 2004, the FASB issued SFAS No. 153, Exchange of Nonmonetary Assets, an amendment of APB Opinion No. 29, Accounting for Nonmonetary Transactions. SFAS No. 153 is based on the principle that exchange of nonmonetary assets should be measured based on the fair market value of the assets exchanged. SFAS No. 153 eliminates the exception of nonmonetary exchanges of similar productive assets and replaces it with a general exception for exchanges of nonmonetary assets that do not have commercial substance. SFAS No. 153 is effective for nonmonetary asset exchanges in fiscal periods beginning after June 15, 2005. Adoption of the provisions of SFAS No. 153 is not expected to have a material impact on Barnwell's financial condition, results of operations, or liquidity.

In March 2005, the FASB issued FASB Interpretation No. 47 (FIN 47), Accounting for Conditional Asset Retirement Obligations, an interpretation of FASB Statement No. 143. FIN 47 clarifies that the term conditional asset retirement obligation as used in FASB Statement No. 143, Accounting for Asset Retirement Obligations, refers to a legal obligation to perform an asset retirement activity in which the timing and (or) method of settlement are conditional on a future event that may or may not be within the control of the entity. Accordingly, an entity is required to recognize a liability for the fair value of a conditional asset retirement obligation if the fair value of the liability can be reasonably estimated. FIN 47 is effective for fiscal years ending after December 15, 2005. Barnwell is evaluating the impact, if any, of FIN 47 on its financial statements.

**11. SUBSEQUENT EVENTS**

On May 11, 2005, Barnwell declared a cash dividend of \$0.06 per share, payable June 15, 2005, to stockholders of record on June 1, 2005.

The Board of Directors approved an increase in the number of authorized shares of the Company from 4,000,000 to 20,000,000 shares in May 2005 and will seek stockholder approval of this increase. The principal reason for the proposed increase in the number of authorized shares is to enable the Company to effectuate a further split of the Company's common stock if, in the judgment of the Company's Board of Directors, a further split is appropriate.

Item 2. Management's Discussion and Analysis or Plan of Operation

**FORWARD-LOOKING STATEMENTS**

This Form 10-QSB contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, including various forecasts, projections of Barnwell's future performance, statements of Barnwell's plans and objectives or other similar types of information. Although Barnwell believes that its expectations are based on reasonable assumptions, it cannot assure that the expectations contained in such forward-looking statements will be achieved. Such statements involve risks, uncertainties and assumptions which could cause actual results to differ materially from those contained in such statements. The risks, uncertainties and other factors that might cause actual results to differ materially from Barnwell's expectations are set forth in the "Forward-Looking Statements" section of Barnwell's annual report on Form 10-KSB for the year ended September 30, 2004. These forward-looking statements speak only as of the date of filing of this Form 10-QSB, and Barnwell expressly disclaims any obligation or undertaking to publicly release any updates or revisions to any forward-looking statements contained herein.

**CRITICAL ACCOUNTING POLICIES AND ESTIMATES**

In response to the Securities and Exchange Commission's Release No. 33-8040, "Cautionary Advice Regarding Disclosure About Critical Accounting Policies," Barnwell identifies its most critical accounting principles upon which its financial reporting is based as the full cost method of accounting for oil and natural gas properties, the accounting for investment in land, the percentage of completion method of accounting for contract drilling, valuation of receivables, the asset and liability method of accounting for deferred income taxes, and the valuation of Barnwell's employee pension plan. The carrying cost of oil and natural gas properties is subject to a valuation ceiling under the full cost method based on estimated future net cash flows from estimated production of proved oil and natural gas reserves, as determined by independent petroleum engineers. Investment in land is subject to a valuation ceiling based on an estimation of the fair value of the property, less costs to sell. The percentage of completion method of accounting for contract drilling is based on estimates of the total costs to complete each contract. Receivables are subject to a valuation ceiling based on estimates of collectible amounts. Deferred tax assets are based on estimates of the realizable value of future tax deductions, which utilize estimates and assumptions regarding future levels of taxable income. Barnwell's accounting for its employee pension plan is based on estimates and assumptions regarding future investment returns, compensation increases, interest rates, and benefit payments. The aforementioned estimates and

assumptions are based on values provided by independent petroleum engineers, in the case of oil and natural gas reserves, on independent actuaries, in the case of pension obligations, or on internal analysis performed by Barnwell's management. Changes in estimates and assumptions affecting any of the above could materially affect Barnwell's reported amounts of assets, liabilities, revenues and expenses. These accounting policies are detailed in the notes to the consolidated financial statements included in Barnwell's annual report on Form 10-KSB for the year ended September 30, 2004 and in relevant sections in this discussion and analysis.

**CONTRACTUAL OBLIGATIONS AND COMMERCIAL COMMITMENTS**

Please see Notes 5, 6, 7, 9 and 11 of the Notes to the Consolidated Financial Statements in Barnwell's annual report on Form 10-KSB for the year ended September 30, 2004. There have been no significant changes in contractual obligations and commercial commitments from September 30, 2004 to March 31, 2005, other than those reported elsewhere in this Form 10-QSB.

**OVERVIEW**

Barnwell is engaged in the following lines of business: 1) oil and natural gas exploration, development, production and sales primarily in Canada (oil and natural gas segment), 2) investment in leasehold land in Hawaii (land investment segment), and 3) drilling wells and installing and repairing water pumping systems in Hawaii (contract drilling segment).

Barnwell sells substantially all of its oil and natural gas liquids production under short-term contracts with marketers of oil. Natural gas sold by Barnwell is generally sold under both long-term and short-term contracts with prices indexed to market prices. The price of natural gas, oil, and natural gas liquids is freely negotiated between buyers and sellers. Market prices for petroleum products are dependent upon factors such as, but not limited to, changes in weather, storage levels, and output. Petroleum prices are very difficult to predict and fluctuate significantly. For example, natural gas prices for Barnwell, based on quarterly averages during the three years ended March 31, 2005, have ranged from a low of \$2.09 per thousand cubic feet to a high of \$5.41 per thousand cubic feet, and tend to be higher in the winter season than in the summer due to increased demand. Oil and natural gas costs generally follow trends in product market prices, thus in times of higher product prices the cost of exploration, development and operation of oil and natural gas properties will tend to escalate as well. Barnwell's oil and natural gas operations makes capital expenditures in the exploration, development, and production of oil and natural gas. Cash outlays for capital expenditures are largely discretionary, however, a minimum level of capital expenditures is required to replace depleting reserves. Due to the nature of oil and natural gas exploration and development, uncertainty exists as to the ultimate success of any drilling effort.

*Barnwell owns a 77.6% controlling interest in Kaupulehu Developments, a Hawaii general partnership which owns interests in leasehold land and development rights for property located approximately six miles north of the Kona International Airport in the North Kona District of the Island of Hawaii, adjacent to and north of the Four Seasons Resort Hualalai at Historic Kaupulehu, between the Queen Kaahumanu Highway and the Pacific Ocean. Kaupulehu Developments' development rights are under option to a developer and revenues are recognized when options are exercised. The remaining options are comprised of six payments of \$2,656,250 due on each December 31 of years 2005 to 2010. In February 2004, Kaupulehu Developments entered into a Purchase and Sale Agreement with WB KD Acquisition LLC (WB) by which Kaupulehu Developments transferred its leasehold interest in*

*approximately 870 acres zoned for resort/residential development, in two increments, to WB. For the first increment, Kaupulehu Developments received an \$11,550,000 cash closing payment in February 2004 and is also entitled to receive monthly interim payments as well as future payments from the buyer based on the following percentages of gross receipts from the developer's sales of single-family residential lots in Increment I: 9% of the gross proceeds from single-family lot sales up to aggregate gross proceeds of \$100,000,000; 10% of such aggregate gross proceeds greater than \$100,000,000 but less than \$300,000,000; and 14% of such aggregate gross proceeds in excess of \$300,000,000. For the second increment, Kaupulehu Developments and WB agreed to use diligent efforts to negotiate, and attempt to document and enter into, prior to the date which is three (3) years following the closing of the sale of the first single-family lot in Increment I, an agreement with regards to the ownership and development of Increment II. The area in which Kaupulehu Developments' interests are located has experienced strong demand for premium residential real estate in recent years, however there is no assurance that any future percentage or development rights payments will be received.*

Barnwell also drills wells and installs and repairs water pumping systems in Hawaii. Contract drilling results are highly dependent upon the quantity, dollar value and timing of contracts awarded by governmental and private entities and can fluctuate significantly. Water well drilling and pump installation activity increased in recent months, although there is no assurance that this trend will continue through the remainder of fiscal 2005 and in future periods.

**RESULTS OF OPERATIONS**





**Summary/General**

*For the three months ended March 31, 2005, Barnwell reported net earnings of \$910,000 as compared to net earnings of \$3,740,000 for the same period in the prior fiscal year. Net earnings for the three months ended March 31, 2005 decreased as net earnings for the prior year period included earnings from the sale of an interest in leasehold land. The February 2004 sale of an interest in leasehold land generated an operating profit, after minority interest, of approximately \$5,200,000. In addition, stock appreciation rights expense increased \$751,000 in the current year period, as compared to the same period last year, due to an increase in the market price of Barnwell's stock. These decreases were partially offset by increases in operating profit generated by both Barnwell's oil and natural gas and contract drilling segments.*

*For the six months ended March 31, 2005, Barnwell reported net earnings of \$3,350,000 as compared to net earnings of \$6,650,000 for the same period in the prior fiscal year. Net earnings for the six months ended March 31, 2005 decreased as net earnings for the prior year period included 1) the aforementioned earnings from the sale of an interest in leasehold land, and 2) a deferred income tax benefit of \$1,540,000 resulting from the enactment of a reduction in Canadian income tax rates. In addition, stock appreciation rights expense increased \$1,426,000 in the current year period, as compared to the same period last year, due to an increase in the market price of Barnwell's stock. The decrease was partially offset by an increase in operating profit generated by Barnwell's oil and natural gas and contract drilling segments.*

*The average exchange rate of the Canadian dollar to the U.S. dollar increased 8% in the three months ended March 31, 2005 as compared to the three months ended March 31, 2004, and 8% in the six months ended March 31, 2005 as compared to the six months ended March 31, 2004. The exchange rate of the Canadian dollar to the U.S. dollar at March 31, 2005 increased 4% as compared to September*

30, 2004. This increase in the value of the Canadian dollar in U.S. dollars increased Barnwell's reported revenues and expenses and assets and liabilities.

### Oil and Natural Gas

The following tables set forth Barnwell's net production and average price per unit of production for the three and six months ended March 31, 2005, as compared to the three and six months ended March 31, 2004. Production amounts reported are net of royalties and the Alberta Royalty Tax Credit.

### SELECTED OPERATING STATISTICS

	Average Prices					
	Three months ended March 31,		Increase			%
	2005	2004	\$			
Natural Gas (MCF)*	\$ 5.41	\$ 4.68	\$ 0.73		16%	
Oil (Bbls)**	\$ 43.46	\$ 31.90	\$ 11.56		36%	
Liquids (Bbls)**	\$ 29.29	\$ 23.78	\$ 5.51		23%	

	Six months ended March 31,					
	2005		2004		Increase	
			\$		%	
Natural Gas (MCF)*	\$ 5.36	\$ 4.38	\$ 0.98		22%	
Oil (Bbls)**	\$ 42.99	\$ 29.56	\$ 13.43		45%	
Liquids (Bbls)**	\$ 29.20	\$ 22.61	\$ 6.59		29%	

	Net Sales Volumes					
	Three months ended March 31,		Increase (Decrease)			%
	2005	2004	Units			
Natural Gas (MCF)*	877,000	822,000	55,000		7%	
Oil (Bbls)**	35,000	40,000	(5,000)		(13)%	
Liquids (Bbls)**	28,000	23,000	5,000		22%	

	Six months ended March 31,					
	2005		2004		Increase (Decrease)	
			Units		%	
Natural Gas (MCF)*	1,817,000	1,644,000	173,000		11%	
Oil (Bbls)**	73,000	80,000	(7,000)		(9)%	
Liquids (Bbls)**	57,000	50,000	7,000		14%	

\*MCF = 1,000 cubic feet

\*\*Bbls = stock tank barrel equivalent to 42 U.S. gallons

*Oil and natural gas revenues increased \$1,509,000 (27%) and \$3,937,000 (37%) for the three and six months ended March 31, 2005, respectively, as compared to the same period in the prior year, due to increases in prices for all petroleum products and increases in natural gas and natural gas liquids net production, partially offset by a decrease in net oil production. Natural gas production increased due to increases in gas production from the Dunvegan area, and gas production from Foley Lake, a new area for Barnwell. Dunvegan gas production increased significantly, 14% and 21% for the three and six months ended March 31, 2005, respectively, which represents 111% and 87% of the natural gas production increase for the three and six months ended March 31, 2005, respectively. Natural gas production declines at various other properties where reserves are maturing partially offset the increases from the Dunvegan and Foley Lake areas. Oil production declined due to maturing reserves, partially offset by an increase in production from the Bonanza area.*

*Oil and natural gas operating expenses decreased \$122,000 (9%) for the three months ended March 31, 2005 and increased \$16,000 (1%) for the six months ended March 31, 2005, as compared to the same periods in the prior year. The decrease for the three months ended March 31, 2005, as compared to the same period in the prior year, was due principally to the receipt of a refund, in the quarter ended March 31, 2005, of approximately \$80,000 in operating expenses overcharged to Barnwell in 2002 and 2003 by the operator of Dunvegan, Barnwell's principal oil and natural gas property (there was no such refund in the prior year period), and higher repairs and maintenance costs incurred in the prior year period as compared to the current year period.*

#### Sale of Interest in Leasehold Land, Sale of Development Rights, and Minority Interest in Earnings

The development rights held by Kaupulehu Developments are for residentially zoned leasehold land within and adjacent to the Hualalai Golf Club and are under option to Kaupulehu Makai Venture, an unrelated entity that is an affiliate of Kajima Corporation of Japan. In December 2004 and 2003, Kaupulehu Makai Venture exercised the portion of its development rights option that was to expire at the end of those months. In both periods, revenue from the option exercise of \$2,656,000 was reduced by \$159,000 of fees related to the sale, resulting in net revenues of \$2,497,000 and a \$1,950,000 operating profit, after minority interest, on the transactions. All capitalized costs associated with Kaupulehu Developments' development rights were expensed in previous years as Barnwell accounts for sales of development rights under option by use of the cost recovery method, therefore there were no other expenses related to the sale. The \$2,497,000 of option revenues is recorded in the Condensed Consolidated Statements of Operations for the three and six months ended March 31, 2005 and 2004 as Sale of development rights, net. The total amount of remaining future option receipts, if all options are fully exercised, is \$15,937,500 as of the date of this filing, comprised of six payments of \$2,656,250 due on each December 31 of years 2005 to 2010. If any annual option payment is not made, the then remaining development right options will expire. There is no assurance that any portion of the remaining options will be exercised.

#### Contract Drilling

Contract drilling revenues and costs increased \$1,542,000 (211%) and \$830,000 (118%), respectively, for the three months ended March 31, 2005, as compared to the same period in the prior year, due to an increase in well drilling work in the current year period. The contract drilling segment generated a \$718,000 operating profit before general and administrative expenses in the three months

ended March 31, 2005, an increase of \$713,000 as compared to a \$5,000 operating profit before general and administrative expenses in the same period of the prior year.

Contract drilling revenues and costs increased \$3,347,000 (325%) and \$1,992,000 (192%), respectively, for the six months ended March 31, 2005, as compared to the same period in the prior year, due to an increase in well drilling work in the current year period. The contract drilling segment generated a \$1,302,000 operating profit before general and administrative expenses in the six months ended March 31, 2005, an increase of \$1,357,000 as compared to a \$55,000 operating loss before general and administrative expenses for the six months ended March 31, 2004.

Contract drilling results for the three and six months ended March 31, 2005 reflected the impact of a recent increase in activity due to an increase in the number and dollar value of recently awarded contracts. Based on contract backlog as of the date of this filing, management estimates that contract drilling operating profit will decline during the remainder of fiscal 2005, as compared to the first half of fiscal 2005. There is no assurance that any future periods will continue to benefit from the aforementioned recent trend in the number and dollar value of contracts awarded.

**Gas Processing and Other**



Gas processing and other income decreased \$268,000 (56%) and \$454,000 (53%) for the three and six months ended March 31, 2005, respectively, as compared to the same periods in the prior year. During the three and six months ended March 31, 2004, Barnwell sold a parcel of vacant land formerly used as a storage and maintenance yard by Barnwell's contract drilling segment. The gain on the sale of the parcel totaled \$139,000 for the three and six months ended March 31, 2004; there was no such sale in the three and six months ended March 31, 2005. In addition, Kaupulehu Developments received \$100,000 and \$250,000 in income related to negotiations on the development of Kaupulehu Developments' resort/residential acreage in the three and six months ended March 31, 2004, respectively; such negotiation revenues discontinued with the consummation of Kaupulehu Developments' sale of an interest in leasehold land in February 2004, therefore there were no such revenues in the three and six months ended March 31, 2005.

**General and Administrative Expenses**

*General and administrative expenses were essentially unchanged (increased \$11,000) for the three months ended March 31, 2005 and increased \$842,000 (17%) for the six months ended March 31, 2005 as compared to the same periods in the prior year. The increases were due to the impact of an increase in Barnwell's stock price on stock appreciation rights, which increased general and administrative expenses by \$751,000 and \$1,426,000 for the three and six months ended March 31, 2005, respectively, as compared to the same periods in the prior year. In addition, professional fees increased \$193,000 for the six months ended March 31, 2005, as compared to the same period in the prior year, due to higher legal and audit fees as a result of increased costs of regulatory compliance, and consulting services related to Barnwell's oil and natural gas leases. Partially offsetting the increase for the three and six months ended March 31, 2005, as compared to the same periods in the prior year, was a decrease in bonuses as \$733,000 of bonuses were issued in the three months ended March 31, 2004 in conjunction with the consummation of Kaupulehu Developments' sale of an interest in leasehold land in February 2004; there were no such bonuses in the three and six months ended March 31, 2005.*

*General and administrative expenses include fees paid to Nearco, Inc., an entity controlled by Mr. Terry Johnston, a director of Barnwell and an indirect 21.8% owner of Kaupulehu Developments, for consulting services related to Kaupulehu Developments leasehold land. Fees paid to Nearco, Inc. totaled \$69,000 and \$148,000 in the three and six months ended March 31, 2005, respectively, and \$69,000 and \$135,000 in the three and six months ended March 31, 2004, respectively. Barnwell believes the fees are fair and reasonable compensation for such services.*

**Depletion, Depreciation and Amortization**

Depletion, depreciation and amortization increased \$424,000 (25%) for the three months ended March 31, 2005, as compared to the same period in the prior year, due to a 13% increase in the depletion rate and a 4% increase in production (in MCF equivalents where one barrel of oil and natural gas liquids are converted to 5.8 MCF equivalents).

Depletion, depreciation and amortization increased \$1,083,000 (34%) for the six months ended March 31, 2005, as compared to the same period in the prior year, due to an 18% increase in the depletion rate and a 7% increase in production (in MCF equivalents where one barrel of oil and natural gas liquids are converted to 5.8 MCF equivalents).

The higher depletion rate in both periods is due to increases in Barnwell's costs of finding and developing proven reserves, and development costs that are incurred to maintain or increase rates of production from reserves found in previous years. Additionally, a portion of the increase in the depletion rate per MCF equivalent for both periods was due to an 8% increase in the average exchange rate of the Canadian dollar to the U.S. dollar. Barnwell's cost of finding and developing proven reserves has increased as a result of the cost of oil and natural gas exploration and development having increased along with product prices, the drilling of unsuccessful wells, and as a portion of recent oil and natural gas capital expenditures were for the development of existing reserves.

#### Income Taxes

In November 2003, Royal Assent was received on a bill passed by the Parliament of Canada, which was then enacted into law, to reduce Canada's corporate tax rate on resource income (income derived from oil and natural gas operations) over a four-year period beginning January 1, 2003 from 29% to 21% with the 21% tax rate commencing on January 1, 2007. Additionally, the bill phases in over the same four-year period tax deductions for royalties, which previously were not tax deductible, and phases out the Resource Allowance deduction along with other changes. Accordingly, during the six months ended March 31, 2004, Barnwell's Canadian deferred income tax liabilities were reduced by approximately \$1,440,000 due to the reduction in Canada's corporate tax rate. There was no benefit attributable to changes in Canada's corporate tax rate on resource income in the three months ended March 31, 2004 or three and six months ended March 31, 2005.

Barnwell's Canadian deferred income tax liabilities were also reduced in the six months ended March 31, 2004 as a result of the Province of Alberta's reduction of the province's corporate tax rate from 13.0% to 12.5%, effective April 1, 2003. The bill was enacted into law in December 2003. The reduction in the tax rate reduced Canadian deferred income taxes liabilities by approximately \$100,000.

in the six months ended March 31, 2004. There were no such changes enacted into law in the three months ended March 31, 2004 or three and six months ended March 31, 2005.

#### Foreign Currency Fluctuations and Other Comprehensive Income

In addition to U.S. operations, Barnwell conducts foreign operations in Canada. Consequently, Barnwell is subject to foreign currency translation and transaction gains and losses due to fluctuations of the exchange rates between the Canadian dollar and the U.S. dollar.

The average exchange rate of the Canadian dollar to the U.S. dollar increased 8% in the three and six months ended March 31, 2005, respectively, as compared to the same periods in the prior year, and the exchange rate of the Canadian dollar to the U.S. dollar increased 4% at March 31, 2005, as compared to September 30, 2004, and remained essentially unchanged at March 31, 2005, as compared to December 31, 2004. Accordingly, the assets, liabilities, stockholders' equity and revenues and expenses of Barnwell's subsidiaries operating in Canada have fluctuated in relationship to such changes in the exchange rate. Barnwell's Canadian dollar assets are greater than its Canadian dollar liabilities; therefore, increases in value of the Canadian dollar to the U.S. dollar generates other comprehensive income, and decreases in value of the Canadian dollar to the U.S. dollar generates an other comprehensive loss. Other comprehensive income (loss) for the three months ended March 31, 2005 was a loss of \$721,000 as compared to other comprehensive loss of \$246,000 for the same period of the prior year. Other comprehensive income for the six months ended March 31, 2005 was \$713,000 as compared to \$563,000 in the same period of the prior year.

Foreign currency transaction gains and losses were not material in the three and six months ended March 31, 2005 and 2004 and are reflected in general and administrative expenses.

The impact of fluctuations of the exchange rates between the Canadian dollar and the U.S. dollar may be material from period to period. Barnwell cannot accurately predict future fluctuations between the Canadian and U.S. dollars.

#### LIQUIDITY AND CAPITAL RESOURCES

*Cash flows provided by operations totaled \$8,801,000 for the six months ended March 31, 2005, an increase of \$8,083,000 as compared to \$718,000 of cash flows provided by operations for the same period in the prior year. The increase was due to higher operating cash flow generated by Barnwell's oil and natural gas and contract drilling segments and timing differences in receivables collections and payables disbursements.*

Cash flows used by investing activities were \$6,802,000 for the six months ended March 31, 2005 as compared to cash provided by investing activities of \$8,613,000 for the six months ended March 31, 2004, a decrease in cash flows of \$15,415,000. The decrease in cash flow is primarily due to Kaupulehu Developments' receipt of a closing payment for the sale of an interest in leasehold land in February 2004 which generated approximately \$10,500,000 of cash, net of associated costs, during the six months ended March 31, 2004; there was no such closing payment received in the six months ended March 31, 2005. In addition, in the six months ended March 31, 2004, Barnwell fully collected a \$1,311,000 note receivable, and received \$440,000 of proceeds, net of associated costs, from the sale of land that was previously utilized as a contract drilling storage yard; there were no such proceeds in the



six months ended March 31, 2005. Capital expenditures increased from \$4,855,000 in the six months ended March 31, 2004 to \$9,087,000 in the six months ended March 31, 2005, an increase of \$4,232,000. Barnwell also invested \$1,800,000 in certificates of deposit at various financial institutions, partially offset by \$1,288,000 of proceeds received on matured certificates of deposit, in the six months ended March 31, 2005, as compared to investments in certificates of deposit of \$1,285,000 in the same period of the prior year. In both periods Barnwell received \$2,497,000, net of expenses, from the sale of development rights.

During the three and six months ended March 31, 2005, Barnwell invested \$4,462,000 and \$8,833,000, respectively, in oil and natural gas properties in Canada, as compared to \$1,506,000 and \$4,615,000 during the same respective periods in the prior year. During the three months ended March 31, 2005, Barnwell participated in the drilling of 26 gross wells (4.2 net wells) in Canada, of which two gross exploratory wells (0.5 net well) were not successful and 24 gross wells (3.7 net wells) are currently being evaluated or appear to be successful. During the six months ended March 31, 2005, Barnwell participated in the drilling of a total of 46 gross wells (8.0 net wells), of which 5 gross wells (1.4 net wells) were not successful and 41 gross wells (6.6 net wells) are currently being evaluated or appear to be successful. The term Gross refers to the total number of wells in which Barnwell owns an interest, and Net refers to Barnwell's aggregate interest therein. For example, a 50% interest in a well represents 1 gross well, but 0.5 net well. The gross figure includes interests owned of record by Barnwell and, in addition, the portion owned by others.

*Management estimates that oil and natural gas capital expenditures for fiscal 2005 will range from \$14,000,000 to \$15,500,000.*

During the six months ended March 31, 2005, Barnwell used \$791,000 of cash flows for financing activities, a \$3,880,000 decrease from \$4,671,000 in the same period of the prior year. In the six months ended March 31, 2005, Barnwell distributed \$513,000 to minority interests resulting from Kaupulehu Developments' property sales, a \$2,120,000 decrease in minority interest distributions from \$2,633,000 during the same period of the prior year as distributions in the prior year included distributions on the aforementioned receipt of a closing payment for the sale of an interest in leasehold land in February 2004. Barnwell also made \$1,293,000 of long-term debt net repayments during the six months ended March 31, 2004, as compared to no long-term debt repayments in the current year. Barnwell paid \$475,000 in dividends during the six months ended March 31, 2005, as compared to \$923,000 in the prior year comparable period, and collected \$197,000 in proceeds from employees' exercise of stock options as compared to \$178,000 in the prior year comparable period.

On December 3, 2004, Barnwell declared a cash dividend of \$0.125 (split-adjusted) per share payable January 5, 2005, to stockholders of record on December 20, 2004.

Also on December 3, 2004, Barnwell declared a two-for-one stock split in the form of a stock dividend. The new shares were distributed on January 28, 2005 to all shareholders of record as of January 11, 2005.

On February 14, 2005, Barnwell declared a cash dividend of \$0.05 per share, post-split, payable March 15, 2005, to stockholders of record on March 1, 2005.

On May 11, 2005, Barnwell declared a cash dividend of \$0.06 per share, payable June 15, 2005, to stockholders of record on June 1, 2005.





The Royal Bank of Canada has renewed Barnwell's credit facility through April 2006 at \$19,000,000 Canadian dollars, or approximately US\$15,700,000 at March 31, 2005. All other terms of the credit facility remained unchanged upon renewal.

At March 31, 2005, Barnwell had \$7,686,000 in cash and cash equivalents and certificates of deposit, and approximately \$5,400,000 of available credit under its credit facility with the Royal Bank of Canada. Barnwell believes its current working capital, future cash flows from operations, land segment sales, and available credit will be sufficient to fund its estimated capital expenditures for at least the next twelve months and meet the repayment schedule on its long-term debt. However, if oil and natural gas production remains at or declines from current levels or oil and natural gas prices decline from current levels, current working capital balances and cash flows generated by operations may not be sufficient to fund Barnwell's current projected level of oil and natural gas capital expenditures, in which case Barnwell may fund capital expenditures with funds generated by land segment sales, long-term debt borrowings, or it may reduce future oil and natural gas capital expenditures.

### **SUBSEQUENT EVENTS**

On May 11, 2005, Barnwell declared a cash dividend of \$0.06 per share, payable June 15, 2005, to stockholders of record on June 1, 2005.

The Board of Directors approved an increase in the number of authorized shares of the Company from 4,000,000 to 20,000,000 shares in May 2005 and will seek stockholder approval of this increase. The principal reason for the proposed increase in the number of authorized shares is to enable the Company to effectuate a further split of the Company's common stock if, in the judgment of the Company's Board of Directors, a further split is appropriate.

### Item 3. Controls and Procedures

As of March 31, 2005, an evaluation was carried out by Barnwell's Chief Executive Officer and Chief Financial Officer of the effectiveness of Barnwell's disclosure controls and procedures. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that Barnwell's disclosure controls and procedures are effective to ensure that information required to be disclosed by Barnwell in reports that it files or submits under the Securities and Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Act of 1934 and the rules thereunder. There was no change in Barnwell's internal control over financial reporting during the quarter ended March 31, 2005, that materially affected, or is reasonably likely to materially affect, Barnwell's internal control over financial reporting.

**PART II. OTHER INFORMATION**

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

(a) The 2005 Annual Meeting of Stockholders of the registrant was held on March 7, 2005.

(b) At the 2005 Annual Meeting the following were elected as directors:

Director	For	Withheld
Morton H. Kinzler	1,257,019	25,698
Alan D. Hunter	1,267,480	15,237
Erik Hazelhoff-Roelfzema	1,258,593	24,124
Martin Anderson	1,267,256	15,461
Murray C. Gardner	1,267,056	15,661
Alexander C. Kinzler	1,261,239	21,478
Terry Johnston	1,256,431	26,286
Russell M. Gifford	1,261,305	21,412
Diane G. Kranz	1,267,360	15,357
Kevin K. Takata	1,269,168	13,549

Item 6. Exhibits and reports on Form 8-K

Exhibits

Exhibit No. 31.1 Rule 13a-14(a) Certification of Chief Financial Officer.

Exhibit No. 31.2 Rule 13a-14(a) Certification of Chief Executive Officer.

Exhibit No. 32 Certification of Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted by Section 906 of the Sarbanes-Oxley Act of 2002.

**SIGNATURE**

In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

BARNWELL INDUSTRIES, INC.  
(Registrant)

/s/ Russell M. Gifford  
Russell M. Gifford  
Executive Vice President and  
Chief Financial Officer

Date: May 11, 2005