ARENA RESOURCES INC
Form 10-Q/A
February 15, 2006

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q/A
Amendment No. 2

(Mark One)
|X| **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the Quarterly Period Ended September 30, 2005

|__| **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANCE ACT OF 1934**
OR
FOR THE TRANSITION PERIOD From __________ to __________.
Commission File Number 001-31657

ARENA RESOURCES, INC.

(Exact name of registrant as specified in its charter)

Nevada	73-1596109
(State or other jurisdiction of Incorporation or organization)	(I.R.S. Employer Identification No.)

4920 South Lewis Street, Suite 107
Tulsa, Oklahoma 74105
(Address of principal executive offices)

(918) 747-6060
(Issuer s telephone number)

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 past 12 months, and (2) has been subject to such filing requirements for the past 90 days. |X| Yes |_| No

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act): |_| Yes |X| No

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

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practical date:

As of October 21, 2005, the Company had outstanding 13,062,452 shares of common stock ($0.001 par value).

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Arena Resources, Inc.
For the Quarter Ended September 30, 2005

Explanatory Note to Amendment No. 2

The purpose of this Amendment No. 2 to the Quarterly Report on Form 10-Q of Arena Resources, Inc. (the Company) for the three and nine months ended September 30, 2005 (the Original Form 10-Q) is to (i) record an adjusted value (adjusted to market value on the date of issuance) of 40,000 shares of the Company s common stock originally issued as a finders fee in connection with the acquisition of property and capitalized as part of our properties subject to amortization, and (ii) restate our financial statements to reflect the change in how we account for compensation expenses associated with options granted to employees under our stock option plan.

Adjusting the capitalized value of our properties subject to amortization was negligible ($35,217) and had no impact on our amortization expenses or net income for the quarter or nine months ended September 30, 2004 or September 30, 2005 as reported in this Form 10-Q.

The change in how we account for compensation expenses associated with options granted to employees essentially results in our recognition of compensation expense related to the discount amount of the exercise price of the option from the market price of the stock at the date of grant over the vesting period. The discount on all options granted through December 31, 2004 has been 15%, and the vesting period has been five years. The result of these changes is that our general and administrative expenses (which include our current compensation expense) for the quarter and nine months ended September 30, 2004 and September 30, 2005 have increased, with a resulting reduction in our net income after taxes. The effect of this change on our net income after taxes is to reduce our net income for the three months ended September 30, 2004 by $26,553 (from $830,049 to $803,496), which results in no change to basic or diluted earnings per share, and for the three months ended September 30, 2005 by $16,208 (from $3,460,207 to $3,443,999), which results in no change to basic or diluted earnings per share, and for the nine months ended September 30, 2004 by $101,683 (from $1,688,239 to $1,586,556), which results in a reduction of our basic earnings per share from $0.23 to $0.21 and to diluted earnings per share from $0.20 to $0.19, and for the nine months ended September 30, 2005 by $59,635 (from $6,505,433 to $6,445,798), which results in a reduction of our basic earnings per share from $0.62 to $0.61 and to diluted earnings per share from $0.54 to $0.53.

Part I Financial Information

Item I. Financial Statements:

The condensed financial statements included herein have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. 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 pursuant to such rules and regulations, although the Company believes that the disclosures are adequate to make the information presented not misleading.

In the opinion of the Company, all adjustments, consisting of only normal recurring adjustments, necessary to present fairly the financial position of the Company and the results of its operations and its cash flows have been made. The results of its operations and its cash flows for the three and nine months ended September 30, 2005 are not necessarily indicative of the results to be expected for the year ending December 31, 2005.

ARENA RESOURCES, INC.
CONDENSED BALANCE SHEETS
(UNAUDITED)
(As Restated Note 2)

	September 30, 2005	December 31, 2004
ASSETS		
Current Assets		
Cash	$ 6,571,237	$ 1,253,969
Accounts receivable	2,902,136	1,149,513
Joint interest billing receivable	28,727	61,805
Prepaid expenses	33,136	33,136
Total Current Assets	9,535,236	2,498,423
Property and Equipment, Using Full Cost Accounting		
Oil and gas properties subject to amortization	53,744,806	34,457,137
Drilling advances	-	900,000
Equipment	26,687	26,687
Office equipment	102,275	60,401
Total Property and Equipment	53,873,768	35,444,225
Less: Accumulated depreciation and amortization	(3,115,915)	(1,565,124)
Net Property and Equipment	50,757,853	33,879,101
Total Assets	$ 60,293,089	$ 36,377,524
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities		
Accounts payable	$ 1,446,884	$ 1,805,865
Accrued liabilities	171,855	34,800
Total Current Liabilities	1,618,739	1,840,665
Long-Term Liabilities		
Notes payable	-	10,000,000
Notes payable to related parties	400,000	400,000
Put option	8,536	95,033
Asset retirement liability	1,370,567	1,267,993
Deferred income taxes	5,691,851	1,971,990
Total Long-Term Liabilities	7,470,954	13,735,016
Stockholders' Equity		
Preferred stock - $0.001 par value; 10,000,000 shares authorized; no shares issued or outstanding	-	-
Common stock - $0.001 par value; 100,000,000 shares authorized; 12,502,827 shares and 9,132,910 shares outstanding, respectively	12,503	9,133
Additional paid-in capital	40,873,792	15,258,352
Options and warrants outstanding	1,454,991	3,213,159
Deferred compensation	(139,164)	(234,277)
Retained earnings	9,001,274	2,555,476
Total Stockholders' Equity	51,203,396	20,801,843

Total Liabilities and Stockholders' Equity	$	60,293,089	$	36,377,524

See the accompanying notes to unaudited condensed financial statements.

ARENA RESOURCES, INC.
CONDENSED STATEMENTS OF OPERATIONS
(UNAUDITED)
(As Restated Note 2)

	For the Three Months Ended September 30, 2005	2004	For the Nine Months Ended September 30, 2005	2004
Oil and Gas Revenues	$ 7,937,785	$ 2,516,970	$ 16,481,074	$ 5,509,784
Costs and Operating Expenses			-	-
Oil and gas production costs	946,380	564,933	2,384,816	1,284,753
Oil and gas production taxes	569,330	192,535	1,230,444	404,268
Depreciation, depletion and amortization	645,908	237,212	1,550,791	553,038
General and administrative expense	285,828	173,969	898,195	635,566
Total Costs and Operating Expenses	2,447,446	1,168,649	6,064,246	2,877,625
Other Income (Expense)				
Gain from change in fair value of put options	20,627	-	86,497	2,905
Accretion expense	(25,158)	(13,007)	(74,484)	(38,072)
Interest expense	(19,266)	(60,296)	(189,541)	(128,407)
Net Other Income (Expense)	(23,797)	(73,303)	(177,528)	(163,574)
Income Before Provision for Income Taxes	5,466,542	1,275,018	10,239,300	2,468,585
Provision for Deferred Income Taxes	(2,022,543)	(471,522)	(3,793,502)	(882,029)
Net Income	$ 3,443,999	$ 803,496	$ 6,445,798	$ 1,586,556
Basic Net Income Per Common Share	0.30	0.10	0.61	0.21
Diluted Net Income Per Common Share	0.27	0.09	0.53	0.19

See the accompanying notes to unaudited condensed financial statements.

ARENA RESOURCES, INC.
CONDENSED STATEMENTS OF CASH FLOWS
(UNAUDITED)
(As Restated Note 2)

For the Nine Months Ended September 30,	2005	2004
Cash Flows From Operating Activities		
Net income	$ 6,445,798	$ 1,586,556
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation, depletion and amortization	1,550,791	553,038
Provision for income taxes	3,793,502	882,029
Gain from change in fair value of put option	(86,497)	(2,905)
Loss on sale of equipment	-	5,585
Amortization of deferred compensation	95,113	162,175
Accretion of discounted liabilities	74,484	38,073
Changes in assets and liabilities:		
Accounts and joint interest receivable	(1,719,545)	(295,218)
Prepaid expenses	-	(4,201)
Accounts payable and accrued liabilities	(295,567)	488,985
Net Cash Provided by Operating Activities	9,858,079	3,414,117
Cash Flows from Investing Activities		
Proceeds from sale of equipment	-	10,500
Cash payments on purchase of East Hobbs	-	(1,028,000)
Purchase and development of oil and gas properties	(18,021,414)	(1,231,668)
Maturity of long term investment	-	25,234
Purchase of office equipment	(41,874)	(18,035)
Net Cash Used in Investing Activities	(18,063,288)	(2,241,969)
Cash Flows From Financing Activities		
Proceeds from issuance of common stock and warrants, net of offering costs	9,916,749	8,434,823
Proceeds from exercise of warrants	13,605,728	189,500
Issuance of notes payable	-	1,000,000
Payment of notes payable	(10,000,000)	(10,008,440)
Net Cash Provided by (Used in) Financing Activities	13,522,477	(384,117)
Net Increase in Cash	5,317,268	788,031
Cash at Beginning of Period	1,253,969	1,076,676
Cash at End of Period	$ 6,571,237	$ 1,864,707
Supplemental Cash Flow Information		
Cash paid for income taxes	$ 73,641	$ -
Cash paid for interest	$ 189,541	$ 131,421
Non-Cash Investing and Financing Activities		
Common stock issued for properties	$ 340,650	$ -
Asset retirement obligation incurred in property acquisition	28,090	-
East Hobbs property was acquired as follows:		
Fair value of assets acquired	$ -	$ 10,295,312
Liabilities assumed	-	(54,319)
Notes payable incurred	-	(9,008,440)

Common stock issued	-	(204,553)
Cash paid		$ 1,028,000

See the accompanying notes to unaudited condensed financial statements.

ARENA RESOURCES, INC.
NOTES TO UNAUDITED CONDENSED FINANCIAL STATEMENTS
SEPTEMBER 30, 2005

NOTE 1 BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES

Condensed Financial Statements The accompanying condensed financial statements have been prepared by the Company and are unaudited. In the opinion of management, the accompanying unaudited financial statements contain all adjustments necessary for fair presentation, consisting of normal recurring adjustments, except as disclosed herein.

The accompanying unaudited interim financial statements have been condensed pursuant to the rules and regulations of the Securities and Exchange Commission; therefore, certain information and disclosures generally included in financial statements have been condensed or omitted. The condensed financial statements should be read in conjunction with the Company s annual financial statements included in its annual report on Form 10-KSB as of December 31, 2004. The financial position and results of operations for the three and nine months ended September 30, 2005 are not necessarily indicative of the results to be expected for the full year ending December 31, 2005.

Nature of Operations The Company owns interests in oil and gas properties located in Oklahoma, Texas, Kansas and New Mexico. The Company is engaged primarily in the acquisition, exploration and development of oil and gas properties and the production and sale of oil and gas.

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

Oil and Gas Properties The Company uses the full cost method of accounting for oil and gas properties. Under this method, all costs associated with acquisition, exploration, and development of oil and gas reserves are capitalized. Costs capitalized include acquisition costs, geological and geophysical expenditures, lease rentals on undeveloped properties and costs of drilling and equipping productive and non-productive wells. Drilling costs include directly related overhead costs. Capitalized costs are categorized either as being subject to amortization or not subject to amortization.

All capitalized costs of oil and gas properties, including the estimated future costs to develop proved reserves and estimated future costs of abandonment and site restoration, are amortized on the unit-of-production method using estimates of proved reserves as determined by independent engineers. Investments in unproved properties and major development projects are not amortized until proved reserves associated with the projects can be determined. The Company evaluates oil and gas properties for impairment at least quarterly. Amortization expense for the nine months ended September 30, 2005 was $1,550,791 based on depletion at the rate of $4.52 per barrel of oil equivalent compared to $553,038 based on depletion at the rate of $3.64 per barrel of oil equivalent for the nine months ended September 30, 2004. These amounts include $13,936 and $8,628 of depreciation on equipment during the nine months ended September 30, 2005 and 2004, respectively.

In addition, capitalized costs are subject to a ceiling test which limits such costs to the estimated present value of future net revenues from proved reserves, discounted at a 10-percent interest rate, based on current economic and operating conditions, plus the lower of cost or fair market value of unproved properties. Consideration received from sales or transfers of oil and gas property is accounted for as a reduction of capitalized costs. Revenue is not recognized in connection with contractual services performed in connection with properties in which the Company holds an ownership interest.

ARENA RESOURCES, INC.
NOTES TO UNAUDITED CONDENSED FINANCIAL STATEMENTS
SEPTEMBER 30, 2005

Income Per Common Share Basic income per common share is computed by dividing net income by the weighted-average number of common shares outstanding during the period. Diluted income per share reflects the potential dilution that could occur if all contracts to issue common stock were converted into common stock, except for those that are anti-dilutive.

Concentration of Credit Risk and Major Customer The Company currently has cash in excess of federally insured limits at September 30, 2005. During the nine months ended September 30, 2005, sales to two customers represented 70% and 14%, respectively. At September 30, 2005, these two customers made up 80% and 9% of accounts receivable, respectively.

Stock-Based Employee Compensation The Company applies the recognition and measurement principles of Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees* (APB 25) and related interpretations in accounting for its stock-based compensation awards to employees. The Company recognizes compensation expense related to the 15% discount amount of the exercise price from the market price of the stock at the date of grant over the five year vesting period of the options. The Company recognized compensation expense for the three months ended September 30, 2005 and 2004 of $25,850 and $42,350, respectively and for the nine months ended September 30, 2005 and 2004 of $95,113 and $162,175, respectively.

Alternately, Statement of Financial Accounting Standards No. 123, *Accounting for Stock-Based Compensation* (SFAS No. 123), allows companies to recognize compensation expense over the related service period based on the grant date fair value of the stock option awards. The following table illustrates the effect on net income and basic and diluted income per common share if the Company had applied the fair value recognition provisions of SFAS No. 123 to stock-based employee compensation:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2005	**2004**	**2005**	**2004**
Net income, as reported	$ 3,443,999	$ 803,496	$ 6,445,798	$ 1,586,556
Add: Stock based employee compensation expense included in net income, net of related tax effects	16,208	26,553	59,635	101,683
Deduct: Total stock-based employee compensation expense determined under the fair value based method for all awards, net of related tax effects	(124,385)	(71,435)	(402,818)	(273,632)
Pro Forma Net Income	$ 3,335,822	$ 758,614	$ 6,102,615	$ 1,414,607
Income per Common Share				
Basic, as reported	$ 0.30	$ 0.10	$ 0.61	$ 0.21
Basic, pro forma	0.29	0.09	0.58	0.19
Diluted, as reported	0.27	0.09	0.53	0.19
Diluted, pro forma	0.26	0.09	0.51	0.17

ARENA RESOURCES, INC.
NOTES TO UNAUDITED CONDENSED FINANCIAL STATEMENTS
SEPTEMBER 30, 2005

NOTE 2 RESTATEMENT OF FINANCIAL STATEMENTS

During 2003, the Company granted nonqualified stock options to directors and employees to purchase 1,000,000 shares of common stock. The exercise price was 85% of the market value of the Company s common stock on the dates issued and the options vest over a five-year period. In reliance upon FASB Interpretation No. 44, *Accounting for Certain Transactions Involving Stock Compensation*, the Company considered the 15% discount from the market price of the Company s common stock to be reasonable in determining the fair value of the common stock and determined that the time permitted for exercise of the stock options was limited to a reasonable period; therefore, the Company did not recognize any stock-based compensation from the grant of these stock options. However, the Company has recently reevaluated its conclusion with regard to the time permitted for exercise of the stock options and has determined that the five year vesting period is not a reasonable period. As a result, the discount from market value is stock-based compensation. The stock-based compensation is being recognized over the five-year vesting period of the options.

In addition, the Company recently determined that it did not recognize 40,000 shares of common stock that were issued as a finder s fee at their fair value during 2004. The fair value of the common stock has been determined by the market value of the Company s common stock on the date the shares were issued. The fair value of the finder s fee was capitalized as part of the acquisition of oil and gas properties subject to amortization.

The Company has restated its financial statements for the three and nine months ended September 30, 2005 and 2004 to reflect the effects of these adjustments. As a result of the restatement, the Company recognized additional compensation expense of $25,850 and $42,350 during the three months ended September 30, 2005 and 2004, respectively and $95,113 and $162,175 during the nine months ended September 30, 2005 and 2004, respectively. The cost of oil and gas properties subject to amortization was increased by of $35,217 and stockholders equity was increased by $228,698 at September 30, 2005. The following tables summarize the effect of the restatement on the financial statements for the reporting period September 31, 2005:

	As Previously Stated	Effect of Restatement	As Restated
For the Three Months Ended September 30, 2005			
General and administrative expense	$ 259,978	$ 25,850	$ 285,828
Income before provision for income taxes	5,492,392	(25,850)	5,466,542
Provision for deferred income taxes	2,032,185	(9,642)	2,022,543
Net income	3,460,207	(16,208)	3,443,999
Basic income per common share	0.30	-	0.30
Diluted income per common share	0.27	-	0.27
For the Three Months Ended September 30, 2004			
General and administrative expense	$ 131,619	$ 42,350	$ 173,969
Income before provision for income taxes	1,317,368	(42,350)	1,275,018
Provision for deferred income taxes	487,319	(15,797)	471,522
Net income	830,049	(26,553)	803,496
Basic income per common share	0.10	-	0.10
Diluted income per common share	0.09	-	0.09

ARENA RESOURCES, INC.
NOTES TO UNAUDITED CONDENSED FINANCIAL STATEMENTS
SEPTEMBER 30, 2005

	As Previously Stated	Effect of Restatement	As Restated
For the Nine Months Ended September 30, 2005			
General and administrative expense	$ 803,082	$ 95,113	$ 898,195
Income before provision for income taxes	10,334,413		