

CASTLEGUARD ENERGY INC  
Form 10QSB  
May 12, 2006

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

FORM 10-QSB

- QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934  
For the Quarterly Period Ended March 31, 2006  
OR  
 TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)  
OF THE SECURITIES EXCHANGE ACT OF 1934  
For the Transition Period from \_\_\_\_\_ to \_\_\_\_\_

COMMISSION FILE NUMBER: 0-5525

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

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

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

17768 Preston Road, Dallas, Texas  
(Address of principal executive offices)

75252  
(Zip Code)

(214) 647-2110  
(Registrant's telephone number, including area code)

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

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

Check whether the issuer (1) has 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

Indicate by check mark if the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act). YES [ ] NO [X]

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12-b of the Exchange Act). YES [ ] NO [X]

At March 31, 2006, there were 17,364,626 Common shares outstanding.

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

CASTLEGUARD ENERGY, INC.

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PART I.

Item 1. FINANCIAL STATEMENTS

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of  
Castleguard Energy, Inc.

We have reviewed the accompanying balance sheet of Castleguard Energy, Inc. as of March 31, 2006, and the related statements of operations, cash flows and stockholders' equity for the three month period then ended.

These financial statements are the responsibility of the Company's management.

We conducted our review in accordance with standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of analytical procedures applied to financial data and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with auditing standards generally accepted in the United States of America, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to the accompanying financial statements in order for them to be in conformity with accounting principles generally accepted in the United States of America.

/s/ Whitley Penn LLP

Dallas, Texas  
May 12, 2006

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CASTLEGUARD ENERGY, INC.

BALANCE SHEETS

ASSETS

March 31,  
2006

December 31,  
2005

(Audited)

(Unaudited)

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Current assets:

Cash and cash equivalents	\$	5,547	\$	8,845
		<u>47,716</u>		<u>34,745</u>

Accounts receivable

Total current assets		53,263		43,590
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		<u>1,197,746</u>		<u>1,175,723</u>
--	--	------------------	--	------------------

Petroleum and natural gas interests, net

		<u>1,251,009</u>		<u>1,219,313</u>
--	--	------------------	--	------------------

TOTAL ASSETS	\$		\$	
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LIABILITIES & STOCKHOLDERS' EQUITY

Current liabilities:

Accounts payable and accrued liabilities	\$	61,008	\$	34,034
--	----	--------	----	--------

Joint interest billings payable to operator		116,934		109,983
---	--	---------	--	---------

		<u>182,423</u>		<u>182,423</u>
--	--	----------------	--	----------------

Current portion of long-term debt

Total current liabilities		360,365		326,440
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		<u>30,327</u>		<u>31,066</u>
--	--	---------------	--	---------------

Deferred income taxes

		<u>390,692</u>		<u>357,506</u>
--	--	----------------	--	----------------

TOTAL LIABILITIES

Stockholders' equity:

Common stock, \$0.001 par value, 50,000,000 shares authorized; 19,226,626 shares issued; 17,364,626 outstanding

	19,227	19,227
--	--------	--------

Paid-in capital	965,826	965,826
-----------------	---------	---------

	<u>(68,736)</u>	<u>(67,246)</u>
--	-----------------	-----------------

Accumulated deficit		)
---------------------	--	---

	916,317	917,807
--	---------	---------

	<u>(56,000)</u>	<u>(56,000)</u>
--	-----------------	-----------------

Treasury stock, 1,862,000 shares at cost	)	)
--	---	---

	<u>860,317</u>	<u>861,807</u>
--	----------------	----------------

Total stockholders' equity

	<u>1,251,009</u>	<u>1,219,313</u>
--	------------------	------------------

TOTAL LIABILITIES & STOCKHOLDERS' EQUITY	\$	\$
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See accompanying notes to financial statements.

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## CASTLEGUARD ENERGY, INC.

STATEMENTS OF OPERATIONS

(Unaudited)

	<u>Three Months Ended</u> <u>March 31,</u>	
	<u>2006</u>	<u>2005</u>
Oil and gas sales	\$ <u>70,559</u>	\$ <u>59,233</u>
Expenses:		
Lease operating expense and taxes	17,016	14,929
Depreciation, depletion and amortization	22,187	25,476
General and administrative	<u>29,986</u>	<u>32,186</u>
	<u>69,189</u>	<u>72,591</u>
Income (loss) from operations	1,370	(13,358)
Interest and financing costs	<u>(3,600)</u>	<u>(3,000)</u>
	)	)

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Loss before income taxes	(2,230)	(16,358)
Benefit for income taxes	<u>(740)</u>	<u>(5,100)</u>
	)	)
Net loss	\$ <u>(1,490)</u>	\$ <u>(11,258)</u>
Basic and diluted earnings (loss) per common share	\$ <u>.00</u>	\$ <u>.00</u>
Weighted average number of common shares outstanding (Thousands)	<u>17,365</u>	<u>17,365</u>

See accompanying notes to financial statements.

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CASTLEGUARD ENERGY, INC.

STATEMENTS OF CASH FLOWS

(Unaudited)

	Three Months Ended	
	<u>March 31,</u>	
	<u>2006</u>	<u>2005</u>

Cash Flows from Operating Activities:

Net loss	\$ (1,490)	\$ (11,258)
Adjustments to reconcile net loss to net cash		

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provided by operating activities:		
Depreciation, depletion and amortization	22,187	25,476
Deferred income taxes	(740)	(5,100)
Change in assets and liabilities:		
Accounts receivable	(12,970)	-
Accounts payable, accrued liabilities and joint interest billings payable to operator	<u>33,925</u>	<u>3,167</u>
Net cash provided by operating activities	<u>40,912</u>	<u>12,285</u>
Cash Flows from Investing Activities:		
Additions to petroleum and natural gas interests	<u>(44,210)</u>	<u>(15,827)</u>
	)	)
Net cash used in investing activities	<u>(44,210)</u>	<u>(15,827)</u>
	)	)
Cash Flows from Financing Activities:		
Payments on long-term debt	<u>-</u>	<u>(7,500)</u>
		)
Net cash used in financing activities	<u>-</u>	<u>(7,500)</u>
		)
Net decrease in cash and cash equivalents	(3,298)	(11,042)
Cash and cash equivalents, beginning of period	<u>8,845</u>	<u>28,458</u>
Cash and cash equivalents, end of period	\$ <u>5,547</u>	\$ <u>17,416</u>
Supplemental information:		
Interest paid	\$ <u>1,241</u>	\$ <u>-</u>



See accompanying notes to financial statements.

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## CASTLEGUARD ENERGY, INC.

STATEMENTS OF STOCKHOLDERS' EQUITY

(Unaudited for year 2006 first quarter)

	<u>Common Stock</u>		Paid-in	Treasury	Retained	Total
	<u>Shares</u>	<u>Amount</u>	<u>Capital</u>	<u>Stock</u>	(Accumulated	Stockholders'
					Deficit)	Equity
Balance, December 31, 2004	19,226,626	\$ 19,227	\$ 965,826	\$ (56,000)	\$ 6,490	\$ 935,543
Net loss, 2005	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(73,736)</u>	<u>(73,736)</u>
					)	)
Balance, December 31, 2005	19,226,626	19,227	965,826	(56,000)	(67,246)	861,807
Net loss, first quarter	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(1,490)</u>	<u>(1,490)</u>
					)	)
Balance, March 31, 2006	<u>19,226,626</u>	<u>\$ 19,227</u>	<u>\$ 965,826</u>	<u>\$ (56,000)</u>	<u>\$ (68,736)</u>	<u>\$ 860,317</u>

See accompanying notes to financial statements.

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CASTLEGUARD ENERGY, INC.

NOTES TO FINANCIAL STATEMENTS

Note 1 - Summary of Significant Accounting Policies and Practices

(a) Description of Business

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

(b) Basis of Presentation

The accompanying financial statements have been prepared assuming the Company will continue as a going concern. The Company has continued to incur net losses which have resulted in an accumulated deficit of \$68,736 at March 31, 2006. The Company had a net loss of \$1,490 and \$11,258 for the three months ended March 31, 2006 and 2005, respectively. At March 31, 2006, current liabilities exceeded current assets by \$307,102.

The ability of the Company to continue as a going concern is dependent on the successful implementation of its business plan, obtaining additional capital, and generating sufficient revenues and cash flows. The financial statements do not include any adjustments that might be necessary if the Company is unable to continue as a going concern.

The time required for the Company to become profitable is highly uncertain, and the Company cannot be assured that it will achieve or sustain profitability or generate sufficient cash flow from operations to meet working capital requirements. If required, the ability to obtain additional financing from other

sources also depends on many factors beyond the control of the Company, including the state of the capital markets and the prospects for business growth. The necessary additional financing may not be available or may be available only on terms that would result in further dilution to the current owners of the Company's common stock. The financial statements do not include any adjustments to reflect the possible effect on recoverability and classification of assets or the amounts and classification of liabilities which may result from the inability of the Company to continue as a going concern.

(c) Net Income (Loss) per Weighted Average Share

Basic net income (loss) per weighted average share is calculated using the weighted average number of shares of common stock outstanding.

(d) Oil and Gas Sales

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

Note 2 - Long-Term Debt

The Company is party to a debt agreement with a commercial bank that provides for a \$2,000,000 term note with an initial borrowing base of \$322,333 which is reduced at the rate of \$21,667 per month. Principal payments of \$21,667 per month are due when the amounts outstanding on this note exceed the borrowing base. At December 31, 2005, the borrowing base was less than the outstanding note balance. Interest is payable monthly at the bank's prime rate (7.25% at December 31, 2005) plus .75 percent. The note is collateralized by all of the Company's oil and gas properties and by a guarantee of the Company's principal stockholder. Debt covenants restrict other debt, pledge of assets, sales of assets, payment of dividends, mergers and changes in ownership.

CASTLEGUARD ENERGY, INC.

NOTES TO FINANCIAL STATEMENTS

On April 7, 2005, the Company negotiated new terms for the agreement which extended its maturity to February 1, 2006, provided for a \$5,000 principal reduction immediately and further reductions of \$7,500 each month beginning July 1, 2005. Not all the scheduled reductions were made as required, and the facility expired on February 1, 2006.

On April 4, 2006, the bank agreed to extend the maturity to May 31, 2006, eliminate the monthly required reductions for October 2005 through January 2006 and reduce the borrowing base to \$182,423, the current balance due.

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

This Quarterly Report on Form 10-QSB includes "forward-looking" statements within the meaning of Section 27a of the Securities Act of 1933, as amended (the "Securities Act"), and section 21e of the Securities Exchange Act of 1934, as amended (the "exchange act"). Specifically, all statements other than statements of historical facts included in this report regarding Castleguard Energy Inc.'s financial position, business strategy and plans and objectives of management of the Company for future operations are forward- looking statements. These forward-looking statements are based on the beliefs of the Company's management as well as assumptions made by and information currently available to the Company's management. When used in this report, the words "anticipate," "believe," "estimate," "expect" and "intend" and words or phrases of similar import, as they relate to the Company or Company management, are intended to identify forward-looking statements. Such statements reflect the current view of the Company with respect to future events and are subject to certain risks, uncertainties and assumptions related to certain factors including, without limitation, price levels for oil and natural gas, concentration of oil and natural gas reserves and production, drilling risks, uncertainty of oil and gas reserves, risks associated with the development of additional revenues and with the acquisition of oil and gas properties and other energy assets, operating hazards and uninsured risks, general economic conditions, governmental regulation, changes in industry practices, marketing risks, one time events and other factors described herein ("cautionary statements"). Although the Company believes that the expectations reflected in such forward-looking statements are reasonable, it can give no assurance that such expectations will prove to have been correct. Based upon changing conditions, should any one or more of these risks or uncertainties materialize, or should any underlying assumptions prove incorrect, actual results may vary materially from those described herein as anticipated, believed, estimated, expected or intended. The Company does not intend to update these forward-looking statements. All subsequent written and oral forward- looking statements attributable to the Company or persons acting on its behalf are expressly qualified in their entirety by the applicable cautionary statements. Reference is made to disclosure regarding "Forward-Looking Statements and Cautionary Statements" included in the Company's Annual Report on Form 10-KSB for the year ended December 31, 2005, which is incorporated herein by reference.

The Company is an independent oil and gas exploration company whose strategic focus is the application of advanced seismic imaging and computer-aided exploration technologies in the systematic search for commercial hydrocarbon reserves, primarily in the states of Texas and Louisiana. The Company attempts to leverage its technical experience and expertise with seismic technology to identify exploration and exploitation projects with significant potential economic return. The Company intends to participate in selected exploration projects as a non-operating, working interest owner, sharing both risk and rewards with its partners. The Company has and will continue to pursue exploration opportunities in regions where the Company believes significant opportunity for discovery of oil and gas exists. By reducing drilling risk through seismic technology, the Company seeks to improve the expected return on investment in its oil and gas exploration projects. The Company attempts to limit capital requirements by forming industry alliances and exchanges a portion of its interest for cash and/or a carried interest in its exploration projects.

CASTLEGUARD ENERGY, INC.

RESULTS OF OPERATIONS

Overall Operations

Mechanical problems and rapid well decline curves have adversely affected production in the Minden Louisiana Field for the last three years. Although some wells have been worked over and production

increased, overall production continues to decline more rapidly than anticipated. The decline has adversely affected revenues and cash flow. In addition, a regulatory action in 2003 to retroactively reduce our share of a former producing well required a payment of \$83,631 which further exacerbated our reduced cash resources. Consequently, in 2003 we farmed out a portion of a new well drilled and in 2005 and 2006 only participated in our share of costs to work over two wells each year. The production declines have resulted in a reduction of our reserves that caused an increase in our rate of depreciation, depletion and amortization (DD&A) during 2005 and 2006. Consequences of the foregoing are described in "Liquidity and Capital Resources".

#### Three Month Periods Ended March 31, 2006 vs. 2005

First quarter 2006 (this year) net loss of \$1,490 (\$.00 per share) is improved from a net loss of \$11,258 (\$.00 per share) in the first quarter of 2005 (last year). The improvement was driven by a 125% increase in oil volumes offset by a 45% decline in natural gas volumes from 2005. Improvement was also helped by price increases for both oil and natural gas. Natural gas sales volumes were 4,329 mcf this year versus 7,840 mcf last year and crude oil production improved to 616 barrels from 274 barrels last year. The production increase was attributable to reworks undertaken in the last quarter of 2005; declining gas volumes continued the trend of the last two years.

Prices for oil production improved to \$61.73 per barrel from \$48.66 per barrel last year; gas prices improved to \$7.53 per mcf this year from \$6.17 per mcf last year.

Revenues for this year improved 19% compared to last year. This year benefited from the increase of volume and price for oil which more than offset declining volumes for gas. Expenses including depreciation, depletion and amortization were down 5% compared to last year. The combination of improved revenues and lower expenses resulted in an 87% improvement in the net loss from last year.

#### LIQUIDITY AND CAPITAL RESOURCES

Capital resources and liquidity have been strained since 2003. Our borrowing arrangement with a commercial bank was revised in 2003 to provide some relief but lower production volumes, less cash flow and our share of workover costs have combined to exceed our cash inflows. The operator of wells in Minden started offsetting our revenues in the fourth quarter of 2004 and continued through today. As a consequence, during the fourth quarter of 2004 we started delaying bill paying and principal reductions on our bank obligation. In early April 2005, we negotiated new terms on the bank debt, to bring the note current with a principal reduction of \$5,000 and a revised maturity of February 1, 2006. Terms provided for principal reductions of \$7,500 per month plus interest beginning July 1, 2005. On April 4, 2006 the bank agreed to extend the maturity to May 31, 2006, and eliminate monthly reductions for October, 2005 through January, 2006 and reduce the borrowing base to \$182,423, the current balance due.

To partially alleviate the cash shortage, the Board of Directors approved the sale of the Company's interest in the Cedar Creek, Alabama property and the sale was closed during the second quarter 2005. Proceeds from the sale were used to pay past due bills from vendors.

CASTLEGUARD ENERGY, INC.

Although we paid amounts due the operator in the third quarter 2005, new billings for the well workovers exceeded our ability to pay, so the operator is still holding our revenues until the balance is paid.

The effect of the foregoing is that cash resources continue to be strained and are expected to remain that way for the foreseeable future. As a consequence, little if any capital is available for any new projects or significant workovers of existing wells. The Board of Directors continues to explore options for the future direction of the Company and on April 20, 2006 engaged Petro Capital Securities, LLC a Dallas-based oil and gas focused merchant bank to assist in exploring alternatives to maximize shareholder value.

Item 3. CONTROLS AND PROCEDURES

(a) Evaluation of disclosure controls and procedures

**We evaluated the effectiveness of our disclosure controls and procedures ("Disclosure Controls") as of the end of the quarter ended March 31, 2006. This evaluation ("Controls Evaluation") was done by the President (Chief Executive Officer) and Chief Financial Officer.**

Disclosure Controls are controls and other procedures that are designed to ensure that information required to be disclosed by us in the reports that we file or submit under the Securities Exchange Act of 1934 ("Exchange Act") is recorded processed, summarized and reported within the time periods specified in the SEC's rules and forms. Disclosure Controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by us in the reports that we file under the Exchange Act is accumulated and communicated to our management, including our CEO and CFO, as appropriate to allow timely decisions regarding required disclosure.

Our management, including our CEO and CFO, does not expect that our Disclosure Controls or our internal controls over financial reporting ("Internal Controls") will prevent all error and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, but not absolute, assurance that the objectives of a control system are met. Further, any control system reflects limitations on resources, and the benefits of a control system must be considered relative to its costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within Castleguard have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of a control. A design of a control system is also based upon certain assumptions about potential future conditions; over time, controls may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and may not be detected.

Based upon the Controls Evaluation, our CEO and CFO has concluded that, subject to the limitations noted above, the Disclosure Controls are effective in providing reasonable assurance that material information relating to Castleguard is made known to management on a timely basis during the period when our periodic reports are being prepared.

(b) Changes in internal controls.

Internal control over financial reporting is a framework incorporating processes designed to assure that transactions are booked properly initially and find their way to the appropriate place on the Company's financial statements. There were no changes in our internal control over financial reporting that occurred during the first quarter of 2006 that have materially affected, or are reasonably likely to materially affect our internal control over financial reporting.

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Part II. Other Information

Item 1. Legal Proceedings

Not Applicable

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

Not Applicable

Item 3. Defaults Upon Senior Securities

Not Applicable

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

Not Applicable

Item 5. Other Information

Not Applicable

Item 6. Exhibits

(a) Exhibits -





