ALTEX INDUSTRIES INC
Form 10KSB
December 02, 2004

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-KSB

[X] Annual report under Section 13 or 15(d) of the Securities Exchange Act of 1934
For the fiscal year ended September 30, 2004

[_] Transition report under Section 13 or 15(d) of the Securities Exchange Act of 1934
For the transition period from ___ to.___.

Commission file number 1-9030

ALTEX INDUSTRIES, INC.
(Name of small business issuer in its charter)

Delaware	84-0989164
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
POB 1057 Breckenridge, CO	80424-1057
(Address of principal executive offices)	(Zip Code)

Issuer's Telephone Number: (303) 265-9312

Securities registered under Section 12(b) of the Exchange Act: None

Securities registered under Section 12(g) of the Exchange Act: Common stock, par value $0.01 per share

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 X No ___

Check if there is no disclosure of delinquent filers in response to Item 405 of Regulation S-B contained in this form, and no disclosure will be contained, to the best of registrant's knowledge, in its definitive proxy or information statements incorporated by reference in Part III of this Form 10-KSB or any amendment to this form 10-KSB. [X]

Issuer's revenue for its most recent fiscal year: $853,000

Aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the average bid and asked price of such common equity as of November 26, 2004: $893,000

Number of shares outstanding of issuer's Common stock as of November 26, 2004: 14,877,117

Transitional Small Business Disclosure Format: Yes ___ No X

"SAFE HARBOR" STATEMENT UNDER THE UNITED STATES
PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995

Statements that are not historical facts contained in this Form 10-KSB are forward-looking statements that involve risks and uncertainties that could cause actual results to differ from projected results. Factors that could cause actual results to differ materially include, among others: general economic conditions; the market price of oil and natural gas; the risks associated with exploration and production in the Rocky Mountain region; the Company's ability to find, acquire, market, develop, and produce new properties; operating hazards attendant to the oil and natural gas business; uncertainties in the estimation of proved reserves and in the projection of future rates of production and timing of development expenditures; the strength and financial resources of the Company's competitors; the Company's ability to find and retain skilled personnel; climatic conditions; availability and cost of material and equipment; delays in anticipated start-up dates; environmental risks; the results of financing efforts; and other uncertainties detailed elsewhere herein.

PART I

ITEM 1. DESCRIPTION OF BUSINESS.

Altex Industries, Inc. (or the "Registrant" or the "Company," each of which terms, when used herein, refer to Altex Industries, Inc. and/or its subsidiary) is a holding company with two full-time employees that was incorporated in Delaware in 1985. Through its operating subsidiary, the Company currently owns interests, including working interests, in productive onshore oil and gas properties, buys and sells producing oil and gas properties, and, to a lesser extent, participates in the drilling of exploratory and development wells, and in recompletions of existing wells.

The Company operates only one producing well and one field currently being abandoned. All other interests are in properties operated by others. A working interest owner in a property not operated by that interest owner must substantially rely on information regarding the property provided by the operator, even though there can be no assurance that such information is complete, accurate, or current. In addition, an owner of a working interest in a property is potentially responsible for 100% of all liabilities associated with that property, regardless of the size of the working interest actually owned.

Through the operators of the properties in which it has an interest, the Company sells produced oil and gas to refiners, pipeline operators, and processing plants. If a refinery, pipeline, or processing plant that purchases the Company's production were taken out of service, the Company could be forced to halt production that is purchased by such refinery, pipeline, or plant. Approximately 78% of the Company's oil and gas sales result from production from one field for which there is only one available gas pipeline system (See Note 4 of Notes to Consolidated Financial Statements below.). If this pipeline system were taken out of service, production of both oil and gas from that field would be halted.

Although many entities produce oil and gas, competitive factors play a material role in the Company's production operations only to the extent that such factors affect demand for and prices of oil and gas and demand for, supply of, and prices of oilfield services. The sale of oil and gas is regulated by Federal, state, and local agencies, and the Company is also subject to Federal, state, and local laws and regulations relating to the environment. These laws and

regulations generally provide for control of pollutants released into the environment and require responsible parties to undertake remediation. The Company regularly assesses its exposure to environmental liability and to reclamation, restoration, and dismantlement expense ("RR&D"), which activities are covered by Federal, state, and local regulation. The Company does not believe that it currently has any material exposure to environmental liability or to RR&D, net of salvage value, although this cannot be assured. (See Management's Discussion and Analysis below.)

2

ITEM 2. DESCRIPTION OF PROPERTY.

WELLS AND ACREAGE: At November 26, 2004, the Company owned no undeveloped acreage, and, to the best knowledge of the Company, none of the wells in which the Company owns an interest is a multiple completion. However, certain wells in which the Company owns an interest do produce from multiple zones. At November 26, 2004, the Company owned working interests in 44 gross (14.18 net) productive oil wells (certain of which produce associated natural gas), no wells producing only natural gas, and 20,000 gross (6,000 net) developed acres. Substantially all of the Company's production is located in Utah and Wyoming. One well accounts for approximately 17% of the Company's oil and gas sales and for approximately 34% of the Company's estimated proved oil reserves. The Company has not reported to, or filed with, any other Federal authority or agency any estimates of total, proved net oil or gas reserves since the beginning of the last fiscal year. For additional information, see Note 7 of Notes to Consolidated Financial Statements below.

Production

	Net Production		Average Price		
Fiscal Year	Oil (Bbls)	Gas (Mcf)	Oil (Bbls)	Gas (Mcf)	Average Production Cost Per Equivalent Barrel ("BOE")
2004	11,000	89,000	$ 37.00	$ 4.44	$ 11.04
2003	13,000	84,000	26.54	4.57	10.74
2002	12,000	97,000	22.45	2.15	8.66

DRILLING ACTIVITY: The Company did not participate in the drilling of any wells during fiscal 2002 (FY02"), fiscal 2003 (FY03"), or fiscal 2004 (FY04").

ITEM 3. LEGAL PROCEEDINGS.

None.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.

None.

PART II

ITEM 5. MARKET FOR COMMON EQUITY AND RELATED STOCKHOLDER MATTERS.

The Company's Common stock is quoted on the OTC Bulletin Board under the symbol "ALTX". Inter-dealer prices provided by the OTC Bulletin Board, which do not include retail mark-up, mark-down, or commission, and may not represent actual transactions, are listed in the table below.

	FY04		FY03	
Quarter	High Bid	Low Bid	High Bid	Low Bid
1	$ 0.12	$ 0.06	$ 0.07	$ 0.05
2	0.14	0.09	0.07	0.05
3	0.16	0.08	0.10	0.06
4	0.10	0.09	0.07	0.05

3

At November 26, 2004, there were approximately 4,600 holders of record of the Company's Common stock, excluding entities whose stock is held by clearing agencies. The Company has not paid a dividend during the last two fiscal years.

Small Business Issuer Purchases of Equity Securities

Period	(a) Total Number of Shares (or Units) Purchased	(b) Average Price Paid per Share (or Unit)	(c) Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans or Programs	(d) Maximum Number (or Approximate Dollar Value Shares (or Units) that Ma Be Purchased Under the P or Programs
July 1, 2004 through July 31, 2004				
August 1, 2004 through August 31, 2004				
September 1, 2004 through September 30, 2004	18,700	$ 0.085		
Total	18,700	$ 0.085		

The Company has no publicly announced plan or program for the purchase of shares. In September 2004 the Company purchased 18,700 shares other than through a publicly announced plan or program in open-market transactions.

ITEM 6. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

FINANCIAL CONDITION

Cash balances increased $17,000 during FY04 because $36,000 cash provided by operating activities was reduced by $7,000 cash for additions to other property and equipment and $12,000 cash used to acquire 141,933 shares of treasury stock. Accounts receivable increased $15,000 because of increased sales.

The Company is completing the restoration of the area that had contained its East Tisdale Field in Johnson County, Wyoming. The Company has removed all equipment from the field and has recontoured and reseeded virtually all disturbed areas in the field. Barring unforeseen events, the Company does not believe that the expense associated with any remaining restoration activities will be material, although this cannot be assured. After its bonds with the state and the Bureau of Land Management are released, the Company does not believe it will have any further liability in connection with the field, although this cannot be assured.

The Company regularly assesses its exposure to both environmental liability and RR&D. The Company does not believe that it currently has any material exposure to environmental liability or to RR&D, net of salvage value, although this cannot be assured.

The Company is currently experiencing modest cash flow from operations in spite of the extraordinarily high levels of oil and gas prices, which levels are unlikely to persist into the long term. Should prices decline materially, and should interest rates on cash balances remain at current levels, then, unless the Company materially increases production by acquiring producing properties or by engaging in successful drilling activities or recompletions, the Company is likely to

experience negative cash flows from operations. With the exception of capital expenditures related to production acquisitions or drilling or recompletion activities, none of which are currently planned, the cash flows that could result from such acquisitions or activities, the current level of prices and interest rates, and declining production levels, the Company knows of no trends, events, or uncertainties that have or are reasonably likely to have a material impact on the Company's short-term or long-term liquidity. Except for cash generated by the operation of the Company's producing oil and gas properties, asset sales, and interest income, the Company has no internal or external sources of liquidity other than its working capital. At November 26, 2004, the Company had no material commitments for capital expenditures.

RESULTS OF OPERATIONS

Oil and gas sales increased 10% from $729,000 in FY03 to $802,000 in FY04 because oil sales increased 18% from $345,000 in FY03 to $407,000 in FY04, and gas sales increased 3% from $384,000 in FY03 to $395,000 in FY04. Oil sales increased because a 15% decrease in barrels sold from 13,000 in FY03 to 11,000 in FY04 was more than offset by a 39% increase in price per barrel from $26.54 in FY03 to $37.00 in FY04. Gas sales increased because a 6% increase in thousands of cubic feet ("MCFs") sold from 84,000 in FY03 to 89,000 in FY04 was offset by a 3% decrease in price per MCF from $4.57 in FY03 to $4.44 in FY04. Production taxes increased 24% from $83,000 in FY03 to $103,000 in FY04 because

of increased sales. Net loss decreased from $24,000 in FY03 to a net gain of $38,000 in FY04 because of increased sales.

LIQUIDITY

OPERATING ACTIVITIES. In FY03 net cash used in operating activities was $16,000, and in FY04 net cash provided by operating activities was $36,000.

INVESTING ACTIVITIES. In FY03 the Company expended $4,000 on additions to other property and equipment, and in FY04 the Company expended $7,000 on additions to other property and equipment.

FINANCING ACTIVITIES. In FY03 the Company expended $1,000 to acquire 14,000 shares of treasury stock, and in FY04 the Company expended $12,000 to acquire 141,933 shares of treasury stock. Between October 1, 2004, and November 26, 2004, the Company acquired 110,200 shares of treasury stock for $11,000.

The Company's revenue and earnings are functions of the prices of oil, gas, and natural gas liquids and of the level of production expense, all of which are highly variable and largely beyond the Company's control. In addition, because the quantity of oil and gas produced from existing wells declines over time, the Company's sales and net income will decline unless rising prices offset production declines or the Company increases its net production by investing in the drilling of new wells, in successful workovers, or in the acquisition of interests in producing oil or gas properties. At current price and interest rate levels, the Company is likely to record a modest net gain. With the exception of unanticipated variations in production levels, unanticipated RR&D, unanticipated environmental expense, and possible changes in oil and gas price levels and interest rates, the Company is not aware of any other trends, events, or uncertainties that have had or that are reasonably expected to have a material impact on net sales or revenues or income from continuing operations.

ITEM 7. FINANCIAL STATEMENTS.

The consolidated financial statements follow the signature page.

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

None.

ITEM 8A. CONTROLS AND PROCEDURES

5

The Company maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in the Company's Exchange Act reports is recorded, processed, summarized, and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to the Company's management, including its Principal Executive Officer and Principal Financial Officer as appropriate, to allow timely decisions regarding required disclosure. Management necessarily applied its judgment in assessing the costs and benefits of such controls and procedures which, by their nature, can provide only reasonable assurance regarding management's control objectives.

Within 90 days prior to the date of this report, the Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the Company's Principal Executive Officer and Principal Financial Officer, of the effectiveness of the design and operation of the

Company's disclosure controls and procedures pursuant to Exchange Act Rule 13a-14. Based upon the foregoing, the Company's Principal Executive Officer and Principal Financial Officer concluded that the Company's disclosure controls and procedures are effective in timely alerting them to material information relating to the Company (including its consolidated subsidiary) required to be included in the Company's Exchange Act reports. There have been no significant changes in the Company's internal controls or in other factors which could significantly affect internal controls subsequent to the date the Company carried out its evaluation.

ITEM 8B. OTHER INFORMATION

None.

PART III

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

Mr. Steven H. Cardin, 54, an economist, formerly with The Conference Board and the consulting firm, National Economics Research Associates, has been Chairman and CEO of the Company for over five years, and a Director since 1984. Mr. Jeffrey S. Chernow, 53, a lawyer, formerly Director of Enforcement in the Division of Securities, State of Maryland, Office of the Attorney General, has been in private practice in Maryland for over five years, and a Director since 1989. Mr. Stephen F. Fante, 48, a CPA, formerly Chairman and CEO of IMS, which provided computerized accounting systems to the oil and gas industry and was a reseller of microcomputer products to the Fortune 1000, and formerly Chairman and CEO of Seca Graphics, Inc., which provided design and mapping services and software to the cable television and telecommunications industries, has been a private investor for the last five years, and a Director since 1989.

The Board of Directors has a separately-designated standing Audit Committee which is comprised of Mr. Fante and Mr. Chernow. The Board of Directors has determined that the Company has at least one Audit Committee Financial Expert serving on its Audit Committee: Mr. Fante is an Audit Committee Financial Expert, and he is independent, as that term is used in Item 7(d)(3)(iv) of Schedule 14A under the Exchange Act.

Messrs. Chernow's, Cardin's, and Fante's terms as Directors continue until their successors are duly elected and qualified. The Company has adopted a code of ethics that applies to its principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions.

6

ITEM 10. EXECUTIVE COMPENSATION.

Each Director who is not also an officer of the Company receives $750 per month for service as a Director. No additional fees are paid for service on Committees of the Board or for attendance at Board or Committee Meetings. In 1998, the Company's two non-executive Directors each purchased 155,544 shares of the Company's Common Stock from the Company at a price of $0.17 per share in exchange for notes receivable from each of $26,500. The notes are non-recourse, secured by the respective shares, bear interest at the Applicable Federal Rate, and due on September 30, 2006. The principal amount of the notes can be paid with shares of the Company's Common Stock. The Company will reimburse the Directors for interest expense related to the notes and will indemnify them against additional tax due as a result of such reimbursement and indemnification.

Mr. Cardin has an Employment Agreement with the Company that was effective October 1, 2001, that has an initial term of five years, and that provides that Mr. Cardin is to receive a base salary of $191,000 per annum, escalating at no less than 5% per annum, and an annual bonus of no less than 10% of the Company's earnings before tax. Pursuant to the agreement, Mr. Cardin purchased from the Company 2,383,615 shares of the Company's Common Stock at a price of $.09375 per share and 1,376,249 shares at a price of $0.06 per share in exchange for a note receivable from him of $306,000. The note is non-recourse, is secured by the shares, bears interest at the Applicable Federal Rate, and is due at the end of the term of the Employment Agreement. The principal amount of the note can be paid with shares of the Company's Common Stock. The Company will reimburse Mr. Cardin for interest expense related to the note and will indemnify him against additional tax due as a result of such reimbursement and indemnification.

The Employment Agreement also provides that, in the event the Company terminates Mr. Cardin's employment by reason of his permanent disability, the Company shall (1) pay Mr. Cardin a total sum, payable in 24 equal monthly installments, equal to 50% of the base salary to which he would have been entitled had he performed his duties for the Company for a period of two years after his termination, less the amount of any disability insurance benefits he receives under policies maintained by the Company for his benefit, and (2) continue to provide Mr. Cardin with all fringe benefits provided to him at the time of his permanent disability for a period of two years following such permanent disability.

The Employment Agreement also provides that, in the event the Company terminates Mr. Cardin's employment in breach of the agreement, or in the event that Mr. Cardin terminates his employment because his circumstances of employment shall have changed subsequent to a change in control, then the Company shall pay Mr. Cardin a lump sum payment equal to the sum of (1) twice Mr. Cardin's base salary during the 12-month period immediately preceding the termination of his employment, (2) the greater of (a) twice any annual bonus paid to or accrued with respect to Mr. Cardin by the Company during the fiscal year immediately preceding the fiscal year in which his employment shall have been terminated or (b) three times his base salary during the 12-month period immediately preceding the termination of his employment, and (3) any other compensation owed to Mr. Cardin at the time of his termination. The agreement also provides that the Company will indemnify Mr. Cardin against any special tax that may be imposed on him as a result of any such termination payment made by the Company pursuant to the agreement.

Under the Employment Agreement, a change in control is deemed to occur (1) if there is a change of one-third of the Board of Directors under certain conditions, (2) if there is a sale of all or substantially all of the Company's assets, (3) upon certain mergers or consolidations, (4) under certain circumstances if another person (or persons) acquires 20% or more of the outstanding voting shares of the Company, or (5) if any person except Mr. Cardin shall own or control half of such outstanding voting shares.

The following table sets forth the dollar value of compensation earned by the Company's CEO, its only executive officer, during the last three fiscal years.

Summary Compensation Table

Annual Compensation

Name and Principal Position	Year	Salary	Bonus	Other Annual Compensation
Steven H. Cardin, CEO	2004	$211,000	4,000	9,000
Steven H. Cardin, CEO	2003	$201,000		10,000
Steven H. Cardin, CEO	2002	$191,000		14,000

Pursuant to his Employment Agreement (See above), Mr. Cardin paid $14,000 in interest to the Company in FY02, $10,000 in interest in fiscal FY03, and $9,000 in interest in FY04. The Company reimbursed him for those payments.

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

The following table sets forth information concerning each person who, as of November 26, 2004, is known to the Company to be the beneficial owner of more than five percent of the Company's Common Stock, and information regarding Common Stock of the Company beneficially owned, as of November 26, 2004, by all Directors and executive officers and by all Directors and executive officers as a group.

Name and Address of Beneficial Owner	Shares of Common Stock Beneficially Owned	Percent of Class
Steven H. Cardin (Director and Executive Officer) POB 1057 Breckenridge CO 80424-1057	7,233,866	48.62%
Jeffrey S. Chernow (Director) POB 1057 Breckenridge CO 80424-1057	155,544	1.05%
Stephen F. Fante (Director) POB 1057 Breckenridge CO 80424-1057	155,544	1.05%
All Directors and Executive Officers as a Group (3 Persons)	7,544,954	50.72%

ITEM 12. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS.

Effective October 1, 2001, the Company entered into a five-year employment agreement with its president which provides for a base salary of $191,000 annually, plus escalations of not less than 5% annually. The agreement contains provisions providing for payments to the president in the event of his

disability or termination of his employment. The agreement also provides that he will receive an annual bonus equal to no less than 10% of the Company's earnings before income tax. Pursuant to the employment agreement, the Company's president has purchased from the Company 2,383,615 shares of the Company's common stock at a price of $.09375 per share and 1,376,249 shares at a price of $0.06 per share in exchange for a $306,000 note receivable. The Company's two non-executive directors have each purchased 155,544 shares of the Company's common stock from the Company at a price of $0.17 per share in exchange for notes receivable from each of $26,500. Each of the three notes is non-recourse, secured by the respective shares, due on September 30, 2006, and bears interest at the Applicable Federal Rate. The principal amount of the notes can be paid with shares of the Company's common stock. The Company will reimburse the president and the directors for interest expense related to the notes, and will indemnify them against additional tax due as a result of such reimbursement and indemnification. The

8

Company recognized $11,000 of both interest income and general and administrative expense related to the notes in 2003 and 2004.

ITEM 13. EXHIBITS

3(i)	Articles of Incorporation - Incorporated herein by reference to Exhibit B to August 20, 19
3(ii)	Bylaws - Incorporated herein by reference to Exhibit C to August 20, 1985 Proxy Statement
10	Summary of Employment Agreement between the Company and Steven H. Cardin, effective Octobe Incorporated herein by reference to Form 10-KSB for fiscal year ended September 30, 2001
14	Code of Ethics - Incorporated herein by reference to Form 10-KSB for fiscal year ended Sep
21	List of subsidiaries - Incorporated herein by reference to Form 10-KSB for fiscal year end
31	Rule 13a-14(a)/15d-14(a) Certifications
32	Section 1350 Certifications

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

AUDIT FEES. Fees billed for annual audits and for reviews of Forms 10-QSB and Forms 8-K: Billed in FY04: $10,900. Billed in FY03: $10,525.

AUDIT-RELATED FEES. None

TAX FEES. Fees billed for preparation of registrant's federal and state income tax returns: Billed in FY04: $2,250. Billed in FY03: $2,000. Fees billed for other tax-related services: None.

ALL OTHER FEES. None.

The registrant does not engage an accountant to render audit or non-audit services unless the engagement is explicitly pre-approved by the registrant's Audit Committee. During FY04 and FY03 no Audit-Related or Other Fees were billed, and all Tax Fees had been pre-approved by the Audit Committee.

9

SIGNATURES

In accordance with Section 13 or 15(d) of the Exchange Act, the registrant

caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

ALTEX INDUSTRIES, INC.

/s/ STEVEN H. CARDIN

By: Steven H. Cardin, CEO

Date: December 1, 2004

In accordance with the Exchange Act, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

/s/ STEVEN H. CARDIN
By: Steven H. Cardin, Director,
Principal Executive Officer,
Principal Financial Officer, and
Principal Accounting Officer

Date: December 1, 2004

/s/ STEPHEN F. FANTE

By: Stephen F. Fante, Director

Date: December 1, 2004

10

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

TO THE BOARD OF DIRECTORS AND STOCKHOLDERS
ALTEX INDUSTRIES, INC.

We have audited the accompanying consolidated balance sheet of Altex Industries, Inc. and subsidiary as of September 30, 2004, and the related consolidated statements of operations, stockholders' equity and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Company as of September 30, 2004, and the results of its operations and its cash flows for the year ended September 30, 2004, in conformity with U.S. generally accepted accounting principles.

Denver, Colorado

November 8, 2004

/S/ COMISKEY & COMPANY
PROFESSIONAL CORPORATION

INDEPENDENT AUDITORS' REPORT

THE STOCKHOLDERS AND BOARD OF DIRECTORS
ALTEX INDUSTRIES, INC.

We have audited the accompanying consolidated statements of operations, stockholders' equity, and cash flows of Altex Industries, Inc. and subsidiary for the year ended September 30, 2003. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the results of operations and cash flows of Altex Industries, Inc. and subsidiary for the year ended September 30, 2003, in conformity with accounting principles generally accepted in the United States of America.

Burdick, Meritt & Associates, P.C.

Denver, Colorado
November 6, 2003

ALTEX INDUSTRIES, INC. AND SUBSIDIARY
CONSOLIDATED BALANCE SHEET
SEPTEMBER 30, 2004

ASSETS

CURRENT ASSETS

Cash and cash equivalents	$ 2
Accounts receivable	
Other receivables	

Other	
Total current assets	2
PROPERTY AND EQUIPMENT, AT COST	
Proved oil and gas properties (successful efforts method) (Notes 6 and 7)	1
Other	
	1
Less accumulated depreciation, depletion, amortization, and valuation allowance	(1
Net property and equipment	
OTHER ASSETS	
	$ 2

LIABILITIES AND STOCKHOLDERS' EQUITY

CURRENT LIABILITIES	
Accounts payable	$
Accrued production costs	
Other accrued expenses	
Total current liabilities	
COMMITMENTS AND CONTINGENCIES (Notes 3, 5, and 6)	
STOCKHOLDERS' EQUITY (Note 3)	
Preferred stock, $.01 par value. Authorized 5,000,000 shares, none issued	
Common stock, $.01 par value. Authorized 50,000,000 shares, 14,987,317 shares issued and outstanding	
Additional paid-in capital	14
Accumulated deficit	(11
Notes receivable from stockholders	
	2
	$ 2

See accompanying notes to consolidated financial statements.

13

ALTEX INDUSTRIES, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF OPERATIONS
YEARS ENDED SEPTEMBER 30, 2004 AND 2003

	2004	2003
REVENUE		
Oil and gas sales	$ 802,000	$ 729,000
Interest (Note 3)	42,000	49,000
Other income (expense)	9,000	(1,000)

	853,000	777,000
COSTS AND EXPENSES		
Lease operating	287,000	290,000
Production taxes	103,000	83,000
General and administrative (Note 3)	417,000	419,000
Depreciation, depletion, and amortization	8,000	9,000
	815,000	801,000
NET EARNINGS (LOSS)	$ 38,000	$ (24,000)
EARNINGS (LOSS) PER SHARE OF COMMON STOCK	*	*
WEIGHTED AVERAGE SHARES OUTSTANDING	15,039,919	15,137,113

* Less than $(0.01) per share

See accompanying notes to consolidated financial statements.

14

ALTEX INDUSTRIES, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
YEARS ENDED SEPTEMBER 30, 2004 AND 2003

	COMMON STOCK SHARES	COMMON STOCK AMOUNT	ADDITIONAL PAID-IN CAPITAL	ACCUMULATED DEFICIT	TREASURY STOCK
BALANCES AT SEPTEMBER 30, 2002	15,143,250	$151,000	14,213,000	(11,787,000)	
Net loss				(24,000)	
Acquisition of treasury stock, 14,000 shares at $0.085 per share					(1,000
Retirement of treasury stock	(14,000)		(1,000)		1,000
BALANCES AT SEPTEMBER 30, 2003	15,129,250	151,000	14,212,000	(11,811,000)	
Net earnings				38,000	
Acquisition of treasury stock, 141,933 shares at $0.085 per share					(12,000
Retirement of treasury stock	(141,933)	(1,000)	(11,000)		12,000
BALANCES AT SEPTEMBER 30, 2004	14,987,317	$150,000	14,201,000	(11,773,000)	

See accompanying notes to consolidated financial statements.

15

ALTEX INDUSTRIES, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS
YEARS ENDED SEPTEMBER 30, 2004 AND 2003

	2004	2003
CASH FLOWS FROM OPERATING ACTIVITIES		
Net earnings (loss)	$ 38,000	$ (24,000)
Adjustments to reconcile net earnings (loss) to net cash provided by (used in) operating activities		
Depreciation, depletion, and amortization	8,000	9,000
Increase in accounts receivable	(15,000)	(58,000)
Decrease (increase) in other receivables	(7,000)	4,000
Decrease in other current assets	8,000	7,000
Decrease in other assets	3,000	12,000
Increase (decrease) in accounts payable	(2,000)	3,000
Increase (decrease) in accrued production costs	(5,000)	13,000
Increase in other accrued expenses	8,000	18,000
Net cash provided by (used in) operating activities	36,000	(16,000)
CASH FLOWS USED IN INVESTING ACTIVITIES		
Additions to other property and equipment	(7,000)	(4,000)
CASH FLOWS USED IN FINANCING ACTIVITIES		
Acquisition of treasury stock	(12,000)	(1,000)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	17,000	(21,000)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	2,097,000	2,118,000
CASH AND CASH EQUIVALENTS AT END OF YEAR	$2,114,000	$2,097,000

See accompanying notes to consolidated financial statements.

16

ALTEX INDUSTRIES, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2004 AND 2003

NOTE 1 - NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES.

NATURE OF OPERATIONS: Altex Industries, Inc., through its wholly-owned subsidiary, jointly referred to as "the Company," owns interests, including working interests, in productive oil and gas properties located in Utah and Wyoming. The Company's revenues are generated from sales of oil and gas production, sales of oil and gas properties, and interest income from cash deposits. The Company's operations are significantly affected by changes in oil and gas prices and in interest rates.

PRINCIPLES OF CONSOLIDATION: The consolidated financial statements include the accounts of Altex Industries, Inc. and its wholly-owned subsidiary. All intercompany balances and transactions have been eliminated in consolidation.

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 and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

PROPERTY AND EQUIPMENT: The Company follows the successful efforts method of accounting for oil and gas operations, under which exploration costs, including geological and geophysical costs, annual delay rentals, and exploratory dry hole costs, are charged to expense as incurred. Costs to acquire unproved properties, to drill and equip exploratory wells that find proved reserves, and to drill and equip development wells are capitalized. Capitalized costs relating to proved oil and gas properties are depleted on the units-of-production method based on estimated quantities of proved reserves and estimated RR&D (Note 6). Upon the sale or retirement of property and equipment, the cost thereof and the accumulated depreciation, depletion, and valuation allowance are removed from the accounts, and the resulting gain or loss is credited or charged to operations. Actual RR&D expense in excess of estimated RR&D expense is charged to operations.

IMPAIRMENT OF LONG-LIVED ASSETS: The Company assesses long-lived assets for impairment when circumstances indicate that the carrying value of such assets may not be recoverable. This review compares the asset's carrying value with management's best estimate of the asset's expected future undiscounted cash flows without interest costs. If the expected future cash flows exceed the carrying value, no impairment is recognized. If the carrying value exceeds the expected future cash flows, an impairment equal to the excess of the carrying value over the estimated fair value of the asset is recognized. No such impairment may be restored in the future. The Company's proved oil and gas properties are assessed for impairment on an individual field basis.

CASH EQUIVALENTS AND FAIR VALUES OF FINANCIAL INSTRUMENTS: For purposes of the statement of cash flows, the Company considers all highly liquid investments with an original maturity of three months or less to be cash equivalents. The carrying amount reported on the balance sheet for cash and cash equivalents approximates its fair value.

INCOME TAXES: The Company follows the asset and liability method of accounting for deferred income taxes. The asset and liability method requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of temporary differences between financial accounting and tax bases of assets and liabilities.

EARNINGS PER SHARE: Earnings per share of common stock is based upon the weighted average number of shares of common stock outstanding during the year.

CONCENTRATIONS OF CREDIT RISK: The Company sells the majority of its oil and gas production to two customers (Note 4). Receivables are not collateralized. Although this concentration could affect the Company's overall exposure to credit risk, management believes the risk is minimal. Although the Company maintains significant amounts of cash, management does not permit cash deposits to exceed federally insured limits with any one institution.

REVENUE RECOGNITION: Substantially all of the Company's revenue is from sales of oil and gas production and from interest income. Revenue from oil and gas production is recognized based on sales or delivery date. Interest income is recognized when earned.

NOTE 2 - INCOME TAXES. At September 30, 2004, the Company had net operating loss and depletion carryforwards for income tax purposes of $323,000 and $1,021,000,

respectively. If not utilized, the net operating losses will expire during the period from 2005 through 2023. The approximate tax effect of each type of temporary difference and carryforward that gives rise to a significant portion of deferred tax assets at September 30, 2004, computed in accordance with SFAS No. 109, is as follows:

DEFERRED TAX ASSETS	
Net operating loss carryforward	$
Depletion carryforward	
Tax basis of assets written off for financial statement purposes	

	1,
DEFERRED TAX LIABILITY	
Depletion, depreciation, amortization, and valuation allowance for income tax purposes in excess of amounts for financial statement purposes	

TOTAL NET DEFERRED TAX ASSETS	1,
Less valuation allowance	(1,

NET DEFERRED TAX ASSET	$

Based on the uncertainty of future realization, a valuation allowance equal to the net deferred tax asset has been provided. Accordingly, no tax benefit has been recorded.

Income tax expense is different from amounts computed by applying the statutory Federal income tax rate for the following reasons:

Tax expense (benefit) at 35% of net earnings (loss)
Change in valuation allowance for net deferred tax assets
Expiration of tax carryforwards
Change in valuation allowance for net deferred tax assets due to an increase in depletion carryforwards
Other

Income tax expense

NOTE 3 - RELATED PARTY TRANSACTIONS. Effective October 1, 2001, the Company entered into a five-year employment agreement with its president which provides for a base salary of $191,000 annually, plus escalations of not less than 5% annually. The agreement contains provisions providing for payments to the president in the event of his disability or termination of his employment. The agreement also provides that he will receive an annual bonus equal to no less than 10% of the Company's earnings before income tax. At September 30, 2001, the Company had accrued bonus expense of $75,000. In 2002 the Company issued 936,868 shares of common stock to the president, valued at $0.08 per share, in lieu of cash, as payment of his accrued bonus. Pursuant to the employment agreement, the

Company's president has purchased from the Company 2,383,615 shares of the Company's common stock at a price of $.09375 per share and 1,376,249 shares at a price of $0.06 per share in exchange for a $306,000 note receivable. The Company's two non-executive directors have each purchased 155,544 shares of the Company's common stock from the Company at a price of $0.17 per share in exchange for notes receivable from each of $26,500. Each of the three notes is non-recourse, secured by the respective shares, due on

September 30, 2006, and bears interest at the Applicable Federal Rate. The principal amount of the notes can be paid with shares of the Company's common stock. The Company will reimburse the president and the directors for interest expense related to the notes, and will indemnify them against additional tax due as a result of such reimbursement and indemnification. The Company recognized $11,000 of both interest income and general and administrative expense related to the notes in 2003 and 2004.

NOTE 4 - MAJOR CUSTOMERS. In 2004 and 2003 the Company had two customers who individually accounted for 10% or more of the Company's oil and gas sales and who, in aggregate, accounted for 95% of oil and gas sales in 2004 and 94% of oil and gas sales in 2003. In 2004 the two customers individually accounted for 78% and 17% of oil and gas sales, and in 2003 the two customers individually accounted for 79% and 15% of oil and gas sales.

NOTE 5 - LEASES. The Company rented office space under a noncancellable operating lease that expired in April 2004 and that the Company renewed for five years ending April 30, 2009. At September 30, 2004, required future payments under the lease are $21,000 for the years ending September 30, 2005, September 30, 2006, September 30, 2007, and September 30, 2008, and $12,000 for the year ending September 30, 2009. In 2004 and 2003 the Company incurred rent expense of $21,000.

NOTE 6 - RECLAMATION, RESTORATION, AND DISMANTLEMENT (RR&D). The Company is completing the restoration of the area that had contained its East Tisdale Field in Johnson County, Wyoming. The Company has removed all equipment from the field and has recontoured and reseeded virtually all disturbed areas in the field. Barring unforeseen events, the Company does not believe that the expense associated with any remaining restoration activities will be material, although this cannot be assured. After its bonds with the state and the Bureau of Land Management are released, the Company does not believe it will have any further liability in connection with the field, although this cannot be assured.

NOTE 7 - SUPPLEMENTAL FINANCIAL DATA - OIL AND GAS PRODUCING ACTIVITIES (UNAUDITED). The Company's operations are confined to the continental United States, and all of the Company's reserves are proved developed. Prices and costs in the tables below have been estimated using prices and costs in effect at the end of the years indicated. Prices are estimated net of estimated quality and transportation adjustments. Income tax expense is not reflected in the tables below because of the anticipated utilization of net operating loss carryforwards and tax credits. The estimation of reserves is complex and subjective, and reserve estimates tend to fluctuate in light of new production data.

I. CAPITALIZED COSTS RELATING TO OIL AND GAS PRODUCING ACTIVITIES

	SEPTEMBER 30, 2004
Proved properties	$ 1,076,000
Accumulated depreciation, depletion, amortization, and valuation allowance	(1,032,000)
Net capitalized cost	$ 44,000

ALTEX INDUSTRIES, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2004 AND 2003

II. ESTIMATED QUANTITIES OF PROVED OIL AND GAS RESERVES

	OIL IN BARRELS	GAS IN MCFS
BALANCE AT SEPTEMBER 30, 2002	90,000	579,000
Revisions of previous estimates	10,000	223,000
Production	(13,000)	(84,000)
BALANCE AT SEPTEMBER 30, 2003	87,000	718,000
Revisions of previous estimates	24,000	120,000
Production	(11,000)	(89,000)
BALANCE AT SEPTEMBER 30, 2004	100,000	749,000

III. PRESENT VALUE OF ESTIMATED FUTURE NET REVENUE

	AT SEPTEMBER 30	
	2004	2003
Estimated future revenue	$ 7,870,000	$ 5,345,000
Estimated future expenditures	(4,990,000)	(3,771,000)
Estimated future net revenue	2,880,000	1,574,000
10% annual discount of estimated future net revenue	(905,000)	(431,000)
Present value of estimated future net revenue	$ 1,975,000	$ 1,143,000

IV. SUMMARY OF CHANGES IN PRESENT VALUE OF ESTIMATED FUTURE NET REVENUE

	YEAR ENDED SEPTEMBER 30	
	2004	2003
Present value of estimated future net revenue, beginning of year	$ 1,143,000	$ 672,000
Sales, net of production costs	(412,000)	(356,000)
Net change in prices and costs of future production	785,000	459,000
Revisions of quantity estimates	383,000	260,000
Accretion of discount	114,000	67,000
Change in production rates and other	(38,000)	41,000
Present value of estimated future net revenue, end of year	$ 1,975,000	$ 1,143,000

EXHIBIT INDEX

31	Rule 13a-14(a)/15d-14(a) Certifications
32	Section 1350 Certifications