

ISRAMCO INC
Form 10-K
March 23, 2012

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

FORM 10-K

Mark one:

- ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934 FOR THE FISCAL YEAR ENDED DECEMBER 31, 2011
- TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934

COMMISSION FILE NUMBER: 0-12500

ISRAMCO, INC.

(Exact name of registrant as specified in its charter)

Delaware 13-3145265
(State or Other Jurisdiction of Incorporation) (IRS Employer Identification No.)

2425 West Loop South, Suite 810, Houston Texas 77027
(Address of Principal Executive Offices)

713-621-6785
(Registrant's Telephone Number, including Area Code)

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
(Title of Class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.
Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the
Act. Yes No

Indicate by check mark whether the issuer (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 (or for such shorter period that the registrant was required

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to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No r

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No r

Indicate by check mark if disclosure of delinquent filers in response to Item 405 of Regulation S-K is not contained in this Form, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.r

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer r Accelerated filer x Non-accelerated filer r Smaller Reporting Company
r

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Securities Exchange Act). Yes r No x

As of March 22, 2012, there were 2,717,691 shares of the Registrant's common stock par value \$0.01 per share ("Common Stock") outstanding. The aggregate market value of the Common Stock held by non-affiliates of the Registrant at March 23, 2012, based on the last sale price of such equity reported on the Nasdaq market, was approximately \$227 million.

DOCUMENTS INCORPORATED BY REFERENCE

Information required by Part III, Items 10, 11, 12, 13 and 14, is incorporated by reference to portions of the registrant's definitive proxy statement for its 2012 annual meeting of stockholders, which will be filed on or before April 30, 2012.

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ISRAMCO, INC.
2011 FORM 10-K ANNUAL REPORT

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Special note regarding forward-looking statements

This report on Form 10-K contains forward-looking statements within the meaning of the federal securities laws. All statements, other than statements of historical facts, concerning, among other things, planned capital expenditures, potential increases in oil and natural gas production, the number of anticipated wells to be drilled in the future, future cash flows and borrowings, pursuit of potential acquisition opportunities, our financial position, business strategy and other plans and objectives for future operations, are forward-looking statements. These forward-looking statements are identified by their use of terms and phrases such as “may,” “expect,” “estimate,” “project,” “plan,” “believe,” “intend,” “achieve,” “anticipate,” “will,” “continue,” “potential,” “should,” “could” and similar terms and phrases. Although we believe that the expectations reflected in these forward-looking statements are reasonable, they do involve certain assumptions, risks and uncertainties. The actual results could differ materially from those anticipated in these forward-looking statements. One should consider carefully the statements under the “Risk Factors” section of this report and other sections of this report that describe factors that could cause our actual results to differ from those set forth in the forward-looking statements, including, but not limited to, the following factors:

- the volatility in commodity prices for oil and natural gas, including continued declines in prices;
- the possibility that the industry may be subject to future regulatory or legislative actions (including any additional taxes and changes in environmental regulation);
- the presence or recoverability of estimated oil and natural gas reserves and the actual future production rates and associated costs;
- the possibility that production decline rates for some of our oil and gas producing properties are greater than we expect;
- our ability to generate sufficient cash flow from operations, borrowings or other sources to enable us to fully develop our undeveloped acreage positions;
- the ability to replace oil and natural gas reserves;
- environmental risks;
- drilling and operating risks;
- exploration and development risks;
- competition, including competition for acreage in oil and gas producing areas and for experienced personnel;
- management’s ability to execute our plans to meet our goals;
- our ability to retain key members of senior management and key technical employees;
- our ability to repay our credit facility when due;
- our ability to obtain goods and services, such as drilling rigs and tubulars, and access to adequate gathering systems and pipeline take-away capacity, to execute our drilling and development programs;
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general economic conditions, whether internationally, nationally or in the regional and local market areas in which we do business, may be less favorable than expected, including the possibility that the current economic recession in the United States will be severe and prolonged, which could adversely affect the demand for oil and natural gas and make it difficult, if not impossible, to access financial markets;

- other economic, competitive, governmental, legislative, regulatory, geopolitical and technological factors that may negatively impact our business, operations or pricing.

Finally, our future results will depend upon various other risks and uncertainties, including, but not limited to, those detailed in the section entitled “Risk Factors” included in this report. All forward-looking statements are expressly qualified in their entirety by the cautionary statements in this paragraph and elsewhere in this document. Other than as required under the securities laws, we do not assume a duty to update these forward-looking statements, whether as a result of new information, subsequent events or circumstances, changes in expectations or otherwise.

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PART I

ITEM 1. BUSINESS

Overview

Istramco, Inc., a Delaware corporation incorporated in 1982 (hereinafter, “we”, the “Company” or “Istramco”), together with its subsidiaries is an independent oil and natural gas company engaged in the exploration, development and production of predominately oil and natural gas properties located onshore in the United States and off shore Israel and operate a well service company that provides well maintenance and workover services, well completion and recompletion services.

At December 31, 2011, our estimated total proved oil, natural gas reserves and natural gas liquids, as prepared by our independent reserve engineering firms, Netherland, Sewell & Associates, Inc and Cawley, Gillespie & Associates, Inc., were approximately 34,990 thousand barrels of oil equivalent (“MBOE”), consisting of 3,234 thousand barrels (MBbls) of oil, and 179,155 million cubic feet (MMcf) of natural gas and 1,896 thousand barrels (MBbls) of natural gas liquids. Approximately 27% of our proved reserves were classified as proved developed (See Note 16 Supplemental Oil and Gas Information to Consolidated Financial Statements to our consolidated financial statements). Full year 2011 production averaged 2.16 MBOE/d compared to 2.3 MBOE/d in 2010.

Our business strategy is to maximize the rate of return on investment of capital by controlling operating and capital costs, acquiring strategic oil and gas properties and improving of existing oil and gas properties. An additional important goal for implementing our business strategy is to maintain the lowest possible operating cost structure, among other things, by serving as operator of a substantial portion of our oil and natural gas properties.

Exploration, Development and Production

United States

We, through our wholly-owned subsidiaries, are involved in oil and gas exploration, developing, production and operation of wells in the United States and the operation of a well service company. We own varying working interests in oil and gas wells in Louisiana, Texas, New Mexico, Oklahoma, Wyoming, Utah and Colorado and currently serve as operator of approximately 589 wells located mainly in Texas and New Mexico.

In August, 2011 we created a new subsidiary and in October began operation of a well service company. We began the operations by acquiring five well services rigs and related equipment.

Israel

In 2007 we closed our branch in Israel in order to focus on our expanding presence in the United States Despite the closure of that branch we retained certain overriding royalties in three oil and gas licenses located offshore Israel, These licenses granted by the government of Israel known as the “Michal”, "Matan" and "Shimson" Licenses.

In 2009, two natural gas discoveries, known as "Tamar" and "Dalit", were made within the area covered by Michal and Matan Licenses, respectively. In December 2009, the Israeli Petroleum Commissioner granted Noble Energy, Inc. (“Noble”) and its partners, Istramco Negev 2-LP, Delek Drilling, Avner Oil & Gas, and Dor Gas (the “Tamar Consortium”), two leases (the “Tamar Lease” and the "Dalit Lease"). The Leases are scheduled to expire on December 2038 and cover the Tamar and Dalit gas fields (collectively the “Tamar Field”). The Tamar Field is approximately 95 kilometers of the coast of the Israel in the Israel exclusive economic zone of the Eastern Mediterranean with a water

depth of approximately 1700 meters.

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During January – March 2012, the Tamar Consortium has executed gas supply contracts for sales of natural gas to five separate industrial customers located in Israel and to the Israel Electricity Company. It is anticipated that gas deliveries under such contracts would begin in mid 2013. The contracts are also subject to certain material conditions precedent. Therefore there can be no assurances that there will be any actual gas deliveries under any of such supply contracts.

We own an overriding royalty interest of 1.5375% in the Tamar Field, which will increase to 2.7375% after payout (collectively the “Tamar Royalty”). An overriding royalty interest is an ownership in a percentage of production or production revenues, free of cost of production or development from the underlying leases. As with most overriding royalty interests, we have no control over the operations, drilling, expenses, or timing of production or sales or any other aspect of development or production of the underlying natural gas.

We have a third party reserve report from independent petroleum engineers, Netherland, Sewell & Associates dated March 21, 2012 and estimating reserves allocable to the Tamar Royalty as of December 31, 2011 (the “Tamar Reserve Report”). This reserve report estimates that by reason of its ownership of the Tamar Royalty, we have proven undeveloped reserves estimated at 154.1 billion cubic feet of natural gas. The Tamar Reserve Report indicates that the undiscounted estimated future net revenue (after deduction of estimated production and ad valorem taxes but before estimated income tax) for such reserves (paid out over time) at \$634,462,200. The Tamar Reserve Report estimates the net present worth of such reserves, discounted at 10% annual discount rate factor, at \$241,737,300 (See Note 16 Supplemental Oil and Gas Information to Consolidated Financial Statements to our consolidated financial statements). The gas price used to value the reserves in the Tamar Reserve Report is the 12-month unweighted arithmetic average of the first-of-the-month Henry Hub spot price for each month in the period January through December 2011. That price of \$4.118 per MMBTU is a hypothetical sales price held constant throughout the estimated life of the reserves allocable to the Tamar Royalty for purposes of the estimate and does not represent any actual sales price or contractual sales price for the gas. The report indicates that there are no commercial oil deposits or condensate that is included as reserves.

The amount of proceeds, if any, we receive from the production of the natural gas will be determined not only by the timing of production and price received but, as our interest increases at payout, the expenses and costs incurred by the operations. Payout is the point when all the cost of leasing, drilling, producing and operating the leases have been recovered from proceeds from production from the leases as defined in the royalty agreement.

As we do not control any of those factors affecting our payments (time of production, price received, costs incurred) for our interest and based on that and the other risk factors as set out herein it is difficult to determine the amounts or timing of any amounts we receive with precision or when payout is likely to occur, if ever. Based on reserves and anticipated production and using the income from these interests may be very significant to the Company, if they can be commercially produced.

Commercial production of such reserves is subject to numerous major risks. These risks will include all of the typical risks associated with offshore oil and gas production. Commercial production of such reserves will also be subject to additional major risks that may be unique to the Tamar Field. These include:

- There has not been any large scale production of natural gas offshore Israel. Therefore there may be geological, geophysical or other unforeseen problems that may be unique to the offshore Israel site that could limit such production. In addition, even if commercial production of the reserves can be achieved, it is uncertain what the likely life of such commercial production is likely to be.
- Even if our reserves can be produced, there are no natural gas pipelines or other suitable transportation modalities that presently exist to transport the natural gas. Therefore, commercial exploitation of the reserves will require

construction of pipelines or other transportation modalities to enable the natural gas to market. The development plan presently contemplates transportation of gas production through a 152 kilometer pipeline through the Tamar Field to Ashdod. There can be no assurance that the pipeline will be completed or completed on a timely basis.

- There has been significant political upheaval and unrest in the Mideast, particularly in Syria, Egypt and other countries near Israel. In addition, there is considerable hostility between Iran and Israel and other countries. There is significant risk that war, acts of terrorism or other force majeure may delay, prevent or destroy commercial production of natural gas from the Tamar Field, thereby diminishing or preventing production of natural gas from the Tamar Field.
- The Tamar Consortium will be required to obtain significant financing to develop and produce the field and build transportation to market. There can be no assurances as to whether such financing will be procured, the timing of the financing or whether the financing will be procured on favorable terms and conditions.
- The market for natural gas in Israel exists but the financial ability of customers of the Tamar Consortium to take and pay for material amounts of such natural gas is unknown

The Company also has an interest in a separate area of the Eastern Mediterranean. Based on a gas find, a 30 year lease covering 53 square kilometers (approximately 13,100 acres) offshore Israel was granted in June 2000 (the "Med Yavne Lease"). The original operator of the Med Yavne Lease was BG International Limited, a member of the British Gas Group ("BG"). BG resigned as the operator of the Lease and relinquished all of its working interests in the Med Yavne Lease. The remaining participants in the lease appointed I.O.C - Israel Oil Company Ltd ("IOC") as the successor operator.

Our participation interest of the Med Yavne Lease is 0.7052 %. We also hold an overriding royalty interest in the Med Yavne Lease of 0.1% before payout and 1.3% after payout. We have no reserves attributed to this interest and this lease may not be capable of being economically produced

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Derivative Instruments and Hedging Activities

We utilize derivative contracts to hedge against the variability in cash flows associated with the forecasted sale of our anticipated future oil and natural gas production. We generally hedge a substantial, but varying, portion of our anticipated oil and natural gas production for the next 48 and 15 months, respectively. We do not use derivative instruments for trading purposes. We have elected not to apply hedge accounting to our derivative contracts, which would potentially allow us to not record the change in fair value of our derivative contracts in the consolidated statements of operations. We carry our derivatives at fair value on our consolidated balance sheets, with the changes in the fair value included in our consolidated statements of operations in the period in which the change occurs. Our results of operations would potentially have been significantly different had we elected and qualified for hedge accounting on our derivative contracts.

As of December 31, 2011 we had swap contracts for a volume of 282,873 barrels of crude oil during 36 months, commencing January 2012, and swap contracts for a volume of 174,222 MMBTU of natural gas during 3 months commencing January 2012.

Hereunder are the open swap contracts positions as of December 31, 2011:

	Swap Contracts			
	Natural Gas		Crude Oil	
	Volume (MMBTU) (*)	Weighted Average Price (\$/MMBTU)	Volume (Bbl)	Weighted Average Price (\$/Bbl)
2012	174,222	8.65	127,473	99.67
2013	-	-	89,400	103.51
2014	-	-	66,000	103.51

(*) Mcf = MMBTU

During the second quarter of 2009, we made the decision to mitigate a portion of our interest rate risk with interest rate swaps. These swap instruments reduce our exposure to market rate fluctuations by converting variable interest rates to fixed interest rates.

Under these swaps, we make payments to, or receive payments from, the counterparties based upon the differential between a specified fixed price and a price related to the three-month LIBOR. These interest rate swaps convert a portion of our variable rate interest on our Scotia debt (as defined in Note 6, "Long-term Debt and Interest Expense") to a fixed rate obligation, thereby reducing the exposure to market rate fluctuations. We have elected to designate these positions for hedge accounting and therefore the unrealized gains and losses are recorded in accumulated other comprehensive loss. The Company measures hedge effectiveness by assessing the changes in the fair value or expected future cash flows of the hedged item.

As of December 31, 2011 we did not have open interest rate swap positions.

On March 9, 2010, pursuant to an agreement with Wells Fargo & Company, the derivative contracts between Isramco and Wells Fargo were terminated and the Company signed new swap contracts with Macquarie Bank, N.A. for an aggregate volume of 336,780 barrels of crude oil during the 46 month period commencing March 2011.

Competitive Conditions in the Business

The oil and natural gas industry is highly competitive and we compete with a substantial number of other companies that have greater financial and other resources. Many of these companies explore for, produce and market oil and natural gas, as well as carry on refining operations and market the resultant products on a worldwide basis. There are also a great many well service companies that compete for the same customers as we compete. The primary areas in which we encounter substantial competition are in locating and acquiring attractive producing oil and natural gas properties, obtaining purchasers and transporters of the oil and natural gas we produce, attracting customers to a new well service business and hiring and retaining key employees during active times in the oil and gas industry. Furthermore, competitive conditions may be substantially affected by various forms of energy legislation and/or regulation considered from time to time by the government of the United States and in some instances individual states where we operate. It is not possible to predict the nature of any such legislation or regulation which may ultimately be adopted or its effects upon our future operations. Such laws and regulations may substantially increase the costs of exploring for, developing or producing oil and natural gas and may prevent or delay the commencement or continuation of a given operation.

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Markets and Major Customers

Through our wholly-owned subsidiary, we operate a substantial portion of our domestic oil and natural gas properties. As the operator of a property, the Company makes full payment of the costs associated with each property and seeks reimbursement from the other working interest owners in the property for their share of those costs. Isramco's joint interest partners consist primarily of independent oil and natural gas producers. If the oil and natural gas exploration and production industry in general were adversely affected, the ability of the Company's joint interest partners to reimburse the Company could be adversely affected.

The purchasers of the Company's oil and natural gas production consist primarily of independent marketers, major oil and natural gas companies and gas pipeline companies. The Company has not experienced any significant losses from uncollectible accounts as to its sales of oil and gas production. The Company does not believe the loss of any one of its purchasers would materially affect the Company's ability to sell the oil and natural gas it produces. The Company believes other purchasers are available in the Company's areas of operations.

Seasonality of Business

Weather conditions affect the demand for, and prices of, natural gas and can disrupt our overall business plans. Demand for natural gas is typically higher in the fourth and first quarters resulting in higher natural gas prices. Due to these seasonal fluctuations, results of operations for individual quarterly periods may not be indicative of the results that may be realized on an annual basis.

Operational Risks

Oil and natural gas exploration and development involves a high degree of risk that even a combination of experience, knowledge and careful evaluation may not be able to overcome. There is no assurance that we will discover or acquire additional oil and natural gas in commercial quantities. Oil and natural gas operations also involve the risk that well fires, blowouts, equipment failure, human error and other circumstances may cause accidental leakage of toxic or hazardous materials, such as petroleum liquids or drilling fluids, into the environment, or cause significant injury to persons or property. Such hazards may also cause damage to or destruction of wells, producing formations, production facilities and pipeline or other processing facilities. In such event, substantial liabilities to third parties or governmental entities may be incurred, the satisfaction of which could substantially reduce available cash and possibly result in loss of oil and natural gas properties.

We carry insurance against such hazards. However, as is common in the oil and natural gas industry, we will not insure fully against all risks associated with our business, either because such insurance is not available or because we believe the premium costs are prohibitive. A loss not fully covered by insurance could have a materially adverse effect on our financial position and results of operations. For further discussion on risks, see Item 1A. Risk Factors.

Regulations

We do not have any offshore operations in the US. However, all of the jurisdictions in which we own or operate oil and natural gas properties regulate exploration for and production of oil and natural gas. These laws and regulations include provisions requiring permits to drill wells and requirements that we obtain and maintain a bond or other security as a condition to drilling or operating wells. Regulations also specify the permitted location of and method of drilling and casing wells, the surface use and restoration of properties upon which wells are drilled, the sourcing and disposal of water used in the drilling and completion process, and the plugging and abandonment of wells.

Our operations are also subject to various conservation laws and regulations. These include the regulation of the size of drilling and spacing units or proration units, the number of wells which may be drilled in a given area, and the unitization or pooling of oil and natural gas properties, as well as regulations that generally prohibit the venting or flaring of natural gas, and impose certain requirements regarding the establishment of maximum allowable rates of production from fields and individual wells. The effect of these regulations is to potentially limit the amount of oil and natural gas that we can produce from our wells and to limit the number of wells or the locations at which we can drill, although we can apply for exceptions to such regulations or to have reductions in well spacing.

Failure to comply with applicable laws and regulations can result in substantial penalties. The regulatory burden on the industry increases the cost of doing business and affects profitability.

Each state in which we operate also imposes some form of production or severance tax with respect to the production and sale of oil, natural gas and natural gas liquids within its jurisdiction. We are liable for paying this tax on our production, and are also liable for various real and personal property taxes on our leases and facilities.

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Environmental and Occupational Health and Safety Regulations

The oil and gas industry in the United States is subject to stringent federal, state and local laws regulating the discharge of materials into the environment or otherwise relating to health and safety or the protection of the environment. Many governmental agencies, such as the United States Environmental Protection Agency (the “EPA”) have issued lengthy and comprehensive regulations to implement and enforce these laws. These laws and regulations often require difficult and costly compliance measures. Failure to comply with these laws and regulations may result in the assessment of substantial administrative, civil and criminal penalties, as well as the issuance of injunctions limiting or prohibiting our activities.

In addition, some laws and regulations relating to protection of the environment may, in certain circumstances, impose strict liability for environmental contamination, rendering a person liable for environmental damages and cleanup costs without regard to negligence or fault on the part of that person. We endeavor to fully comply with these regulatory requirements; however, compliance increases our costs and consequently affects our profitability.

As a part of the overall environmental regulatory policy, the permitting, construction and operations of certain oil and gas facilities are regulated. Many factors, including public perception, can materially impact the ability to secure an environmental construction or operation permit. Once operational, enforcement measures can include significant civil penalties for regulatory violations, regardless of intent. Under appropriate circumstances, an administrative agency can issue a cease and desist order to require termination of operations.

Environmental regulation is becoming more comprehensive and additional programs, as well as increased obligations under existing programs, are anticipated. In this regard, we expect additional regulation of naturally occurring radioactive materials, oil and natural gas exploration and production operations, waste management, and underground injection of water and waste material. The adoption of additional regulations could have a material adverse effect on our financial condition and results of operations. Environmental laws and regulations have been subject to frequent changes over the years, and the imposition of more stringent requirements could have a material adverse effect on our financial condition and results of operations.

Comprehensive Environmental Response, Compensation and Liability Act and Hazardous Substances

In 1980, the United States Congress enacted the federal Comprehensive Environmental Response, Compensation and Liability Act, referred to as CERCLA or the Superfund law. This law, which has been amended since enactment, and comparable state laws impose strict liability, without regard to fault, on certain classes of persons that are considered to be responsible for the release of what are considered to be “hazardous substances” into the environment. These persons include the current or former owners or operators of the sites where the release occurred and companies that disposed or arranged for the disposal of hazardous substances released at the site. Under CERCLA, we may be subject to joint and several liability for the costs of investigating and cleaning up hazardous substances that have been released into the environment whether or not we are responsible for the release or even owned the site at the time of the release, as well as for damages to natural resources and for the costs of health studies. In addition, companies that incur liability frequently confront additional claims because it is not uncommon for neighboring landowners and other third parties to file claims for personal injury and property damage allegedly caused by hazardous substances or other pollutants released into the environment.

The Solid Waste Disposal Act and Waste Management

The federal Solid Waste Disposal Act, as amended by the Resource Conservation and Recovery Act of 1976, referred to as RCRA, regulates the disposal of solid waste but generally excludes most wastes generated by the exploration and production of oil and natural gas, such as drilling fluids, produced waters and other wastes associated with the

exploration, development or production of oil and natural gas from regulation as hazardous wastes. However, these wastes may be regulated by the EPA or state agencies as non-hazardous wastes as long as these wastes are not commingled with regulated hazardous wastes. Moreover, in the ordinary course of our operations, other wastes generated in connection with our exploration and production activities may be regulated as hazardous waste under RCRA or hazardous substances under CERCLA. From time to time, releases of materials or wastes have occurred at locations we own or at which we have operations. These properties and the materials or wastes released thereon may be subject to CERCLA, RCRA and analogous state laws. Under these laws, we have been and may be required to remove or remediate these materials or wastes. At this time it is not possible to estimate the potential liabilities to which we may be subject from unknown, latent liability risks with respect to any properties where materials or wastes may have been released, but of which we have not been made aware.

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The Clean Water Act, wastewater and storm water discharges

The oil and gas industry, and our operations, are also subject to the federal Clean Water Act and analogous state laws. Under the Clean Water Act, the EPA has adopted regulations concerning discharges of storm water runoff. This program requires covered facilities to obtain individual permits, or seek coverage under a general permit. Some of our properties may require permits for discharges of storm water runoff and, as part of our overall evaluation of our current operations, we may apply for storm water discharge permit coverage and updating storm water discharge management practices at some of our facilities. We believe that we will be able to obtain, or be included under, these permits, where necessary, and be required make only minor modifications to existing facilities and operations that would not have a material effect on us. The Clean Water Act and similar state acts regulate other discharges of wastewater, oil, and other pollutants to surface water bodies, such as lakes, rivers, wetlands, and streams. Failure to obtain permits for such discharges could result in civil and criminal penalties, orders to cease such discharges, and costs to remediate and pay natural resources damages.

These laws also require the preparation and implementation of Spill Prevention, Control, and Countermeasure Plans in connection with on-site storage of significant quantities of oil. More specifically, we are required to develop and maintain a plan applicable to each of our properties at which any significant volume of crude oil or other substance is stored and to ensure the site has sufficient protections (such as berms, etc.) to ensure that any spill will be contained and not reach navigable waters.

The Safe Drinking Water Act, groundwater protection, and the Underground Injection Control Program

The federal Safe Drinking Water Act (SWDA), the Underground Injection Control (UIC) program promulgated under the SWDA and state programs all regulate the drilling and operation of salt water disposal wells. EPA directly administers the UIC program in some states and in others the responsibility for the program has been delegated to the state. This program requires that a permit be obtained before drilling salt water disposal well. Monitoring the integrity of well casing must also be conducted periodically to ensure the casing is not leaking saltwater to groundwater. Violation of these regulations and/or contamination of groundwater by oil and natural gas drilling, production, and related operations may result in fines, penalties, and remediation costs, among other sanctions and liabilities under the SWDA and state laws. In addition, third party claims may be filed by landowners and other parties claiming damages for alternative water supplies, property damages, and bodily injury.

We have not heretofore engaged in extensive hydraulic fracturing or other well stimulation services on the wells for which we are the operator and when we do we engage third parties to conduct these operations on our behalf.

The Clean Air Act

The federal Clean Air Act, enacted in 1970, and comparable state laws regulate emissions of various air pollutants through air emissions permitting programs and the imposition of other requirements. The EPA has developed and continues to develop stringent regulations under the authority of the Clean Air Act governing emissions of toxic air pollutants from specified sources. Federal and state regulatory agencies can impose administrative, civil and criminal penalties for non-compliance with air permits or other requirements of the federal Clean Air Act and associated state laws and regulations.

Some of our operations are located in areas designated as “non-attainment” areas, which are geographic areas that do not meet the federal air quality standards. Air emission controls and requirements in non-attainment areas are generally more stringent than those imposed in other areas, and the construction of new, or expansion of existing, sources may be restricted.

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Climate change legislation and greenhouse gas regulation

The issue of “global warming” has attracted significant attention and many believe that emissions of certain gases contribute to this problem. Many nations have agreed to limit emissions of “greenhouse gases” pursuant to the United Nations Framework Convention on Climate Change, and the “Kyoto Protocol.” Methane, a primary component of natural gas, and carbon dioxide, a byproduct of the burning of oil, natural gas, and refined petroleum products, are considered “greenhouse gases” regulated by the Kyoto Protocol. Although the United States is not participating in the Kyoto Protocol, several states have adopted legislation and regulations to reduce emissions of greenhouse gases. Restrictions on emissions of methane or carbon dioxide that may be imposed in various states could adversely affect our operations and demand for our products.

In summary, we may be subject to EPA greenhouse gas monitoring and reporting rules, and potentially new EPA permitting rules if adopted, that would apply greenhouse gas permitting obligations and emissions limitations under the federal Clean Air Act. Whether or not any federal greenhouse gas regulations are enacted, more than one-third of the states have begun taking action on their own to control and/or reduce emissions of greenhouse gases. Several multi-state programs have been developed or are in the process of being developed, including the Regional Greenhouse Gas Initiative involving 10 Northeastern states, the Western Climate Initiative involving seven western states, and the Midwestern Greenhouse Gas Reduction Accord involving seven states. The latter two programs have several other states acting as observers and they may join one of the programs at a later date. Any of the climate change regulatory and legislative initiatives described above could have a material adverse effect on our business, financial condition, and results of operations.

The National Environmental Policy Act

Oil and natural gas exploration and production activities on federal lands are subject to the National Environmental Policy Act, or NEPA. NEPA requires federal agencies, including the Department of the Interior, to evaluate major agency actions that have the potential to significantly impact the environment. In the course of such evaluations, an agency will prepare an Environmental Assessment that assesses the potential direct, indirect and cumulative impacts of a proposed project and, if necessary, will prepare a more detailed Environmental Impact Statement that may be made available for public review and comment. All of our current exploration and production activities, as well as proposed exploration and development plans, on federal lands require governmental permits that are potentially subject to the requirements of NEPA. This process has the potential to delay the development of oil and natural gas projects.

Threatened and endangered species, migratory birds, and natural resources

Various state and federal statutes prohibit certain actions that adversely affect endangered or threatened species and their habitat, migratory birds, wetlands, and natural resources. These statutes include the Endangered Species Act, the Migratory Bird Treaty Act, the Clean Water Act and CERCLA. The United States Fish and Wildlife Service may designate critical habitat and suitable habitat areas that it believes are necessary for survival of threatened or endangered species. A critical habitat or suitable habitat designation could result in further material restrictions to federal land use and private land use and could delay or prohibit land access or development. Where takings of or harm to species or damages to wetlands, habitat, or natural resources occur or may occur, government entities or at times private parties, may act to prevent oil and gas exploration activities or seek damages for harm to species, habitat, or natural resources resulting from drilling, construction or releases of oil, wastes, hazardous substances or other regulated materials, and may seek compensation for alleged natural resources damages and in some cases, criminal penalties.

Hazard communications and community right to know

We are subject to federal and state hazard communications and community right to know statutes, including, but not limited to, the federal Emergency Planning and Community Right-to- Know Act, and regulations. These regulations govern record keeping and reporting of the use and release of hazardous substances.

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Occupational Safety and Health Act

We are subject to the requirements of the federal Occupational Safety and Health Act, commonly referred to as OSHA, and comparable state statutes that regulate the protection of the health and safety of workers. In addition, the OSHA hazard communication standard requires that information be maintained about hazardous materials used or produced in operations and that this information be provided to employees, state and local government authorities and the public.

Hydraulic Fracturing

There have been several regulatory and governmental initiatives to restrict the hydraulic-fracturing process, which could have an adverse impact on our completion or production activities. The U.S. Environmental Protection Agency (EPA) has asserted federal regulatory authority pursuant to the Safe Drinking Water Act over certain hydraulic-fracturing practices notwithstanding the existence of current oil and gas regulations adopted at the state level. Moreover, the EPA has commenced a study of the potential environmental effects of hydraulic fracturing on drinking water and groundwater, with final results expected to be available by 2014. The EPA has also announced plans to propose effluent limitations for the treatment and discharge of wastewater resulting from hydraulic-fracturing activities by 2014. Certain other governmental reviews are either underway or being proposed that focus on environmental aspects of hydraulic-fracturing practices, including evaluations by the U.S. Department of Energy and the DOI, and coordination of an administration-wide review of these practices by the White House Council on Environmental Quality. Congress is currently considering, and has from time to time in the past considered, bills that would regulate hydraulic fracturing and/or require public disclosure of chemicals used in the hydraulic-fracturing process. A number of states, including states in which we operate, have adopted or are considering legal requirements that could impose more stringent permitting, public disclosure, and well-construction requirements on hydraulic-fracturing activities.

These laws and their implementing regulations, as well as state counterparts, generally restrict the level of pollutants emitted to ambient air, discharges to surface water, and disposals or other releases to surface and below-ground soils and ground water. Failure to comply with these laws and regulations may result in the assessment of sanctions, including administrative, civil, and criminal penalties; the imposition of investigatory, remedial, and corrective action obligations or the incurrence of capital expenditures; the occurrence of delays in the development of projects; and the issuance of injunctions restricting or prohibiting some or all of the Company's activities in a particular area. Compliance with these laws and regulations also, in most cases, requires new or amended permits that may contain new or more stringent technological standards or limits on emissions, discharges, disposals, or other releases in association with new or modified operations. Application for these permits can require an applicant to collect substantial information in connection with the application process, which can be expensive and time-consuming. In addition, there can be delays associated with public notice and comment periods required prior to the issuance or amendment of a permit as well as the agency's processing of an application. Many of the delays associated with the permitting process are beyond the control of the Company.

Many states where the Company operates also have, or are developing, similar environmental laws, regulations, or analogous controls governing many of these same types of activities. While the legal requirements may be similar in form, in some cases the actual implementation of these requirements may impose additional, or more stringent, conditions or controls that can significantly alter or delay the development of a project or substantially increase the cost of doing business.

The ultimate financial impact arising from environmental laws and regulations is neither clearly known nor determinable as new standards, such as air emission standards and water quality standards, continue to evolve. However, environmental laws and regulations, including those that may arise to address concerns about global climate

change and the threat of adverse impacts to groundwater arising from hydraulic-fracturing activities, are expected to continue to have an increasing impact on the Company's operations.

Employees

As of December 31, 2011, we had 62 full-time employees. We hire independent contractors on an as needed basis. We have no collective bargaining agreements with our employees. We believe that our employee relationships are satisfactory.

Available Information

We file annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, proxy statements and other documents with the SEC under the Securities Exchange Act of 1934, as amended. The public may read and copy any materials that we file with the SEC at the SEC's Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. Also, the SEC maintains an internet website that contains reports, proxy and information statements, and other information regarding issuers, including Isramco, Inc., that file electronically with the SEC. The public can obtain any document we file with the SEC at www.sec.gov.

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ITEM 1A. RISK FACTORS

In addition to the other information contained in this Annual Report on Form 10-K, investors should consider carefully the following risk factors, which may not be the only risks we face, as our business and operations may also be subject to risks that we do not yet know of, or that we currently believe are immaterial. If any of the events or circumstances described below actually occurs, our business, financial condition or results of operations could be materially and adversely affected and the trading price of our common stock could decline.

Oil, natural-gas and NGLs prices are volatile. A substantial or extended decline in prices could adversely affect our financial condition and results of operations.

Prices for oil, natural gas and NGLs ((Natural Gas Liquids) can fluctuate widely. Our revenues, operating results and future growth rates are highly dependent on the prices we receive for our oil, natural gas and NGLs. Historically, the markets for oil, natural gas and NGLs have been volatile and may continue to be volatile in the future. For example, in recent years market prices for natural gas in the United States have declined substantially from the highs achieved in 2008 and the rapid development of shale plays throughout North America has contributed significantly to this trend. Factors influencing the prices of oil, natural gas and NGLs are beyond our control. These factors include, among others:

- the worldwide military and political environment, uncertainty or instability resulting from the escalation or additional outbreak of armed hostilities or further acts of terrorism in the United States, or elsewhere, particularly Israel;
- worldwide and domestic supplies of crude oil, natural gas and NGLs;
- actions taken by foreign oil and gas producing nations;
- the level of global crude oil and natural gas inventories;
- the price and level of foreign imports of oil, natural gas and NGLs;
- the effect of worldwide energy conservation efforts;
- the price and availability of alternative and competing fuels;
- the cost of exploring for, developing, producing, transporting, and marketing oil, natural gas, and NGLs;
- the availability of pipeline capacity and infrastructure;
- the availability of crude oil transportation and refining capacity;
- consumer demand for oil, gas and NGLs;
- the growth of consumer product demand in emerging markets, such as India and China;
- labor unrest in oil and natural gas producing regions;
- regional pricing differentials;
- weather conditions;
- electricity dispatch;
- domestic and foreign governmental regulations and taxes; and
- the overall economic environment.

The long-term effect of these and other factors on the prices of oil, natural gas and NGLs are uncertain. Prolonged or substantial declines in these commodity prices may have the following effects on our business:

- adversely affecting our financial condition, liquidity, ability to finance planned capital expenditures and results of operations;
- reducing the amount of oil, natural gas and NGLs that we can produce economically;
- causing us to delay or postpone some of our capital projects;

- reducing our revenues, operating income and cash flows;
- reducing the carrying value of our crude oil and natural gas properties;
- reducing the amounts of our estimated proved oil and natural-gas reserves;
- reducing the standardized measure of discounted future net cash flows relating to oil and natural-gas reserves; and
- limiting our access to sources of capital, such as equity and long-term debt.

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Our domestic operations are subject to governmental risks that may impact our operations.

Our domestic operations have been, and at times in the future may be, affected by political developments and are subject to complex federal, state, tribal, local and other laws and regulations such as restrictions on production, permitting, changes in taxes, deductions, royalties and other amounts payable to governments or governmental agencies, price or gathering-rate controls, hydraulic fracturing and environmental protection regulations. In order to conduct our operations in compliance with these laws and regulations, we must obtain and maintain numerous permits, approvals and certificates from various federal, state, tribal and local governmental authorities. We may incur substantial costs in order to maintain compliance with these existing laws and regulations. In addition, our costs of compliance may increase if existing laws, including environmental and tax laws, and regulations are revised or reinterpreted, or if new laws and regulations become applicable to our operations. For example, currently proposed federal legislation, that, if adopted, could adversely affect our business, financial condition and results of operations, includes the following:

- Climate Change Congress has considered climate-change legislation that would seek to reduce emissions of green-house gases (GHGs) through establishment of a “cap-and-trade” plan. It is not possible at this time to predict whether or when Congress may re-introduce or act on climate-change legislation. The U.S. Environmental Protection Agency (EPA) has made findings that emissions of GHGs present a danger to public health and the environment and, based on these findings, has adopted regulations that restrict emissions of GHGs under existing provisions of the federal Clean Air Act, including one that requires a reduction in emissions of GHGs from motor vehicles and another that requires certain construction and operating permit reviews for GHG emissions from certain large stationary sources. In addition, the EPA has adopted rules requiring the monitoring and reporting of GHGs from certain sources, including, among others, onshore and offshore oil and natural-gas production facilities, which includes certain of our operations, on an annual basis. We are monitoring GHG emissions from our operations in accordance with the GHG emissions reporting rule and believe that our monitoring activities are in substantial compliance with applicable reporting obligations.
- Taxes. The U.S. President’s Fiscal Year 2013 Budget Proposal includes provisions that would, if enacted, make significant changes to U.S. tax laws. These changes include, but are not limited to, (i) eliminating the immediate deduction for intangible drilling and development costs, (ii) eliminating the deduction from income for domestic production activities relating to oil and natural-gas exploration and development, and (iii) implementing certain international tax reforms.
- Hydraulic Fracturing is an essential and common practice used to stimulate production of natural gas and/or oil from dense subsurface rock formations such as shales that generally exist between 4,000 and 14,000 feet below ground. We apply hydraulic-fracturing techniques in some of our U.S. onshore oil and natural-gas drilling and completion programs. The process involves the injection of water, sand, and additives under pressure into a targeted subsurface formation. The water and pressure create fractures in the rock formations, which are held open by the grains of sand, enabling the oil or natural gas to flow to the wellbore. The process is typically regulated by state oil and natural-gas commissions; however, the EPA, recently asserted federal regulatory authority over certain hydraulic-fracturing activities involving diesel under the Safe Drinking Water Act and has begun the process of drafting guidance documents related to this newly asserted regulatory authority. In November 2011, the EPA announced its intent to develop and issue regulations under the Toxic Substances Control Act to require companies to disclose information regarding the chemicals used in hydraulic fracturing. In February 2012, the DOI released draft regulations governing hydraulic fracturing on federal and Indian oil and gas leases to require disclosure of information regarding the chemicals used in hydraulic fracturing, advance approval for well-stimulation activities, mechanical integrity testing of casing, and monitoring of well-stimulation operations. In addition, Congress, from time to time, has considered adopting legislation intended to provide for federal regulation of hydraulic fracturing and to require disclosure of the chemicals used in the

hydraulic-fracturing process. In the event that a new, federal level of legal restrictions relating to the hydraulic-fracturing process are adopted in areas where we currently or in the future plan to operate, we may incur additional costs to comply with such federal requirements that may be significant in nature, and also could become subject to additional permitting requirements and experience added delays or curtailment in the pursuit of exploration, development, or production activities.

Certain states in which we operate, including, Louisiana, Texas, and Wyoming, have adopted, and other states are considering adopting, regulations that could impose new or more stringent permitting, disclosure, and additional well-construction requirements on hydraulic-fracturing operations. For example, Texas adopted a law in June 2011 requiring disclosure to the Railroad Commission of Texas and the public of certain information regarding the components used in the hydraulic-fracturing process. In addition to state laws, local land use restrictions, such as city ordinances, may restrict or prohibit drilling in general and/or hydraulic fracturing in particular. We believe that we follow applicable standard industry practices and legal requirements for groundwater protection in our hydraulic fracturing activities. Nonetheless, in the event state or local restrictions are adopted in areas where we are currently conducting, or in the future plan to conduct operations, we may incur additional costs to comply with such requirements that may be significant in nature, experience delays or curtailment in the pursuit of exploration, development, or production activities, and perhaps be limited or precluded in the drilling of wells or in the amounts that we are ultimately able to produce from our reserves.

There are also certain governmental reviews either underway or being proposed that focus on environmental aspects of hydraulic-fracturing practices. The White House Council on Environmental Quality is coordinating an administration-wide review of hydraulic-fracturing practices, and a committee of the U.S. House of Representatives has conducted an investigation of hydraulic-fracturing practices. The EPA has commenced a study of the potential environmental effects of hydraulic fracturing on drinking water and groundwater, with initial results expected to be available by late 2012 and final results by 2014. Moreover, the EPA is developing effluent limitations for the treatment and discharge of wastewater resulting from hydraulic-fracturing activities and plans to propose these standards by 2014. In addition, the U.S. Department of Energy is conducting an investigation into practices the agency could recommend to better protect the environment from drilling using hydraulic-fracturing completion methods. Also, the DOI is considering disclosure requirements or other mandates for hydraulic fracturing on federal lands. These ongoing or proposed studies, depending on any meaningful results obtained, could spur initiatives to further regulate hydraulic fracturing under the Safe Drinking Water Act or other regulatory mechanisms.

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The recent adoption of derivatives legislation by the U.S. Congress could have an adverse effect on the Company's ability to use derivative instruments to reduce the effect of commodity price, interest rate and other risks associated with its business.

The Dodd-Frank Wall Street Reform and Consumer Protection Act (HR 4173), signed into law in 2010, establishes, among other provisions, federal oversight and regulation of the over-the-counter derivatives market and entities, such as the Company, that participate in that market. The new legislation required the Commodities Futures Trading Commission ("CFTC") and the Securities and Exchange Commission (SEC) to promulgate rules and regulations implementing the new legislation within 360 days from the date of enactment. In July 2010, the CFTC granted temporary exemptive relief from certain swap regulation provisions of the legislation until December 21, 2011, or until the agency finalized the corresponding rules. In December 2011, the CFTC extended the potential latest expiration date of the exemptive relief to July 16, 2012. In its rulemaking under the new legislation, the CFTC has issued a final rule on position limits for certain futures and option contracts in the major energy markets and for swaps that are their economic equivalents. Certain bona fide hedging transactions or positions are exempt from these position limits. It is not possible at this time to predict when the CFTC will finalize other regulations, including critical rulemaking on the definition of "swap", "swap dealer" and "major swap participant." Depending on the Company's classification, the financial reform legislation may require the Company to comply with margin requirements and with certain clearing and trade-execution requirements in connection with its derivative activities. The financial reform legislation may also require the counterparties to the Company's derivative instruments to spin off some of their derivatives activities to separate entities, which may not be as creditworthy as the current counterparties. The new legislation and any new regulations could significantly increase the cost of derivative contracts (including through requirements to post collateral which could adversely affect our available liquidity), materially alter the terms of derivative contracts, reduce the availability of derivatives to protect against risks the Company encounters, reduce the Company's ability to monetize or restructure its existing derivative contracts, and increase the Company's exposure to less creditworthy counterparties. If the Company reduces its use of derivatives as a result of the legislation and regulations, the Company's results of operations may become more volatile and its cash flows may be less predictable, which could adversely affect the Company's ability to plan for and fund capital expenditures. Finally, the legislation was intended, in part, to reduce the volatility of oil and natural-gas prices, which some legislators attributed to speculative trading in derivatives and commodity instruments related to oil and natural gas. The Company's revenues could therefore be adversely affected if a consequence of the legislation and regulations is to lower commodity prices. Any of these consequences could have a material adverse effect on the Company's consolidated financial position, results of operations, or cash flows.

Oil and gas drilling is a speculative activity and risky.

We are engaged in the business of oil and natural gas exploration, production and operations and the development of productive oil and gas wells. Our growth will be materially dependent upon the success of future drilling. Drilling for oil and gas involves numerous risks, including the risk that no commercially productive oil or natural gas reservoirs will be encountered. The cost of drilling, completing and operating wells is substantial and uncertain, and drilling operations may be curtailed, delayed or cancelled as a result of a variety of factors beyond our control, including unexpected drilling conditions, pressure or irregularities in formations, equipment failures or accidents, adverse weather conditions, compliance with governmental requirements and shortages or delays in the availability of drilling rigs or crews and the delivery of equipment. Although we believe that the use of 3-D seismic data and other advanced technology should increase the probability of success of our wells and should reduce average finding costs through elimination of prospects that might otherwise be drilled solely on the basis of 2-D seismic data and other traditional methods, drilling remains an inexact and speculative activity. In addition, the use of 3-D seismic data and such technologies requires greater pre-drilling expenditures than traditional drilling strategies and we could incur losses because of such expenditures. Our future drilling activities may not be successful and, if unsuccessful, such failure could have an adverse effect on our future results of operations and financial condition. Although we may discuss

drilling prospects that have been identified or budgeted for, we may ultimately not lease or drill these prospects within the expected time frame, or at all. We may identify prospects through a number of methods, some of which do not include interpretation of 3-D or other seismic data. The drilling and results for these prospects may be particularly uncertain. The final determination with respect to the drilling of any scheduled or budgeted wells will be dependent on a number of factors, including (i) the results of exploration efforts and the acquisition, review and analysis of the seismic data, (ii) the availability of sufficient capital resources and the other participants for the drilling of the prospects, (iii) the approval of the prospects by other participants after additional data has been compiled, (iv) economic and industry conditions at the time of drilling, including prevailing and anticipated prices for oil and natural gas and the availability of drilling rigs and crews, (v) our financial resources and results (vi) the availability of leases and permits on reasonable terms for the prospects and (vii) the payment of royalties to lessors. There can be no assurance that these projects can be successfully developed or that the wells discussed will, if drilled, encounter reservoirs of commercially productive oil or natural gas. There are numerous uncertainties in estimating quantities of proved reserves, including many factors beyond our control.

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Failure to fund continued capital expenditures could adversely affect our properties.

Our acquisition, exploration, and development activities require substantial capital expenditures. Historically, we have funded our capital expenditures through a combination of cash flows from operations and loans from commercial banks and related parties. Future cash flows are subject to a number of variables, such as the level of production from existing wells, prices of crude oil and natural gas, and our success in finding, developing and producing new reserves. If revenues were to decrease as a result of lower crude oil and natural gas prices or decreased production, and our access to capital were limited, we would have a reduced ability to replace our reserves, resulting in a decrease in production over time. If our cash flows from operations are not sufficient to meet our obligations and fund our capital budget, we may not be able to access debt, equity or other methods of financing on an economic basis to meet these requirements, particularly in the current economic environment. If we are not able to fund our capital expenditures, interests in some properties might be reduced or forfeited as a result.

Poor general economic, business or industry conditions may have a material adverse effect on our results of operations, liquidity and financial condition.

Recently, concerns over inflation, energy costs, geopolitical issues, the availability and cost of credit, the United States mortgage market and a declining real estate market in the United States have contributed to increased economic uncertainty and diminished expectations for the global economy.

These factors, combined with volatile oil, natural-gas and NGLs prices, declining business and consumer confidence, and increased unemployment, have precipitated an economic slowdown and a recession. Concerns about global economic conditions have had a significant adverse impact on global financial markets and commodity prices. If the economic climate in the United States or abroad continues to deteriorate, or if an economic recovery is slow or prolonged, demand for petroleum products could continue to diminish or stagnate, which could impact the price at which we can sell our oil, natural gas and NGLs, affect our vendors', suppliers' and customers' ability to continue operations, and ultimately adversely impact our results of operations, liquidity and financial condition.

Estimates of proved oil and natural gas reserves are uncertain and any material inaccuracies in these reserve estimates will materially affect the quantities and the value of our reserves.

There are numerous uncertainties inherent in estimating quantities of proved reserves, including many factors beyond our control that could cause the quantities and net present value of our reserves to be overstated or understated. The reserve information included or incorporated by reference in this report represents estimates prepared by our independent reserve engineering firms; Netherland, Sewell & Associates and Cawley, Gillespie & Associates, Inc. Estimation of reserves is not an exact science. Estimates of economically recoverable oil and natural-gas reserves and of future net cash flows depend on a number of variable factors and assumptions, any of which may cause actual results to vary considerably from these estimates, such as:

- historical production from an area compared with production from similar producing areas;
- assumed effects of regulation by governmental agencies and court rulings;
- assumptions concerning future oil and natural-gas prices, future operating costs and capital expenditures;
- estimates of future severance and excise taxes, workover, and remedial costs.

Estimates of reserves based on risk of recovery and estimates of expected future net cash flows prepared by different engineers, or by the same engineers at different times, may vary substantially. Actual production, revenues, and expenditures with respect to our reserves will likely vary from estimates, and the variance may be material. The discounted cash flows included in this report should not be construed as the fair value of the estimated oil, natural-gas, and NGLs reserves attributable to our properties. For the December 31, 2011, 2010, and 2009 reserves, in accordance with SEC requirements, the estimated discounted future net cash flows from proved reserves are based on average 12-month sales prices using the average beginning-of-month price, while reserves for all periods prior to December 31, 2009, are based on year-end sales prices. Actual future prices and costs may differ materially from the SEC regulation-compliant prices used for purposes of estimating future discounted net cash flows from proved reserves.

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Discoveries or Acquisitions of reserves are needed to avoid a material decline in reserves and production.

The production rates from oil and gas properties generally decline as reserves are depleted, while related per unit production costs generally increase, due to decreasing reservoir pressures and other factors. Therefore, our estimated proved reserves and future oil, gas and NGL production will decline materially as reserves are produced unless we conduct successful exploration and development activities or, through engineering studies, identify additional producing zones in existing wells, secondary or tertiary recovery techniques, or acquire additional properties containing proved reserves. Consequently, our future oil, gas and NGL production and related per unit production costs are highly dependent upon our level of success in finding or acquiring additional reserves.

There is a possibility that we will lose the leases to our oil and gas properties.

Our oil and gas revenues are generated through oil and gas leases. These leases are conditioned on the performance of certain obligations, primarily the obligation to produce oil and/or gas or engage in operations designed to result in the production of oil and gas. If production ceases and operations are not commenced within a specified time, the lease may be lost. The loss of our leases may have a material impact on our revenues.

In the case of Israeli-based properties, we have interests in licenses that, subject to certain conditions, may result in leases being granted. The leases are subject to certain obligations and are renewable at the discretion of various governmental authorities. As such, if the parties responsible for operations are not able to fulfill their obligations under the leases, the leases may be modified, cancelled, not renewed, or renewed on terms different from the current leases. The modification or cancellation of our leases could eliminate our interests and may have a material impact on our revenues.

Our business is highly competitive.

The oil and natural gas industry is highly competitive in many respects, including identification of attractive oil and natural gas properties for acquisition, drilling and development, securing financing for such activities and obtaining the necessary equipment and personnel to conduct such operations and activities. In seeking suitable opportunities, we compete with a number of other companies, including large oil and natural gas companies and other independent operators with greater financial resources, larger numbers of personnel and facilities, and with more expertise. There can be no assurance that we will be able to compete effectively with these entities.

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Poor general economic, business, or industry conditions may have a material adverse effect on our results of operations, liquidity, and financial condition.

During the last few years, concerns over inflation, energy costs, geopolitical issues, the availability and cost of credit, the U.S. mortgage market, uncertainties with regard to European sovereign debt, and a declining real estate market in the United States have contributed to increased economic uncertainty and diminished expectations for the global economy. Concerns about global economic conditions have had a significant adverse impact on global financial markets and commodity prices. If the economic recovery in the United States or abroad remains prolonged, demand for petroleum products could diminish or stagnate, which could impact the price at which we can sell our oil, natural gas, and NGLs, affect our vendors', suppliers' and customers' ability to continue operations, and ultimately adversely impact our results of operations, liquidity, and financial condition.

Our commercial lenders have liens on substantially all of our oil and gas assets in the United States and could foreclose in the event that we default under our credit facilities.

Under the terms of our credit facilities with our commercial lenders, our lenders have a first priority lien on substantially all of our oil and gas assets in the United States. If we default under the credit facility, our lender would be entitled to, among other things, foreclose on our assets in order to satisfy our obligations under a credit facility.

Our hedging activities may prevent us from benefiting fully from price increases and may expose us to other risks.

In order to manage our exposure to price risks in the marketing of our oil and natural gas production, we have entered into oil and natural gas price hedging arrangements with respect to a portion of our anticipated production and we may enter into additional hedging transactions in the future. While intended to reduce the effects of volatile oil and natural gas prices, such transactions may limit our potential gains and increase our potential losses if oil and natural gas prices were to rise substantially over the price established by the hedge. In addition, such transactions may expose us to the risk of loss in certain circumstances, including instances in which:

- our actual production is less than hedged volumes;
- there is a widening of price differentials between delivery points for our production and the delivery point assumed in the hedge arrangement; or
- the counterparties to our hedging agreements fail to perform under the contracts.
- a sudden unexpected event materially impacts oil and natural-gas prices.

The credit risk of financial institutions could adversely affect us.

We have exposure to different counterparties, and we have entered into transactions with counterparties in the financial services industry, including commercial banks, insurance companies and other institutions. These transactions expose us to credit risk in the event of default of our counterparty. Deterioration in the credit markets may impact the credit ratings of our current and potential counterparties and affect their ability to fulfill their existing obligations to us and their willingness to enter into future transactions with us. We have exposure to these financial institutions through our derivative transactions. In addition, if any lender under our credit facility is unable to fund its commitment, our liquidity will be reduced by an amount up to the aggregate amount of such lender's commitment under our credit facility.

We have no means to market our oil and gas production without the assistance of third parties.

The marketability of our production depends upon the proximity of our reserves to, and the capacity of, facilities and third party services, including oil and natural gas gathering systems, pipelines, trucking or terminal facilities, and processing facilities. The unavailability or lack of capacity of such services and facilities could impair or delay the production of new wells or the delay or discontinuance of development plans for properties. A shut-in, delay or discontinuance could adversely affect our financial condition. In addition, regulation of oil and natural gas production transportation in the United States or in other countries may affect its ability to produce and market our oil and natural gas on a profitable basis.

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The unavailability or high cost of drilling rigs, equipment, supplies, personnel and oil field services could adversely affect our ability to execute our exploration and development plans on a timely basis and within our budget.

Our industry is cyclical and, from time to time, there is a shortage of drilling rigs, equipment, supplies and/or qualified personnel. During these periods, the costs and delivery times of rigs, equipment and supplies are substantially greater. In addition, the demand for, and wage rates of, qualified drilling rig crews rise as the number of active rigs in service increases. Increasing levels of exploration and production in response to strong prices of oil and natural gas may increase the demand for oilfield services, and the costs of these services may increase, while the quality of these services may suffer.

Our oil and natural gas activities are subject to various risks that are beyond our control.

Our operations are subject to many risks and hazards incident to exploring and drilling for, producing, transporting, marketing and selling oil and natural gas. Although we may take precautionary measures, many of these risks and hazards are beyond our control and unavoidable under the circumstances. Many of these risks or hazards could materially and adversely affect our revenues and expenses, the ability of certain of our wells to produce oil and natural gas in commercial quantities, the rate of production and the economics of the development of, and our investment in the prospects in which we have or will acquire an interest. Any of these risks and hazards could materially and adversely affect our financial condition, results of operations and cash flows. Such risks and hazards include:

- human error, accidents, labor force and other factors beyond our control that may cause personal injuries or death to persons and destruction or damage to equipment and facilities;
- blowouts, fires, hurricanes, pollution and equipment failures that may result in damage to or destruction of wells, producing formations, production facilities and equipment;
- unavailability of materials and equipment;
- engineering and construction delays;
- unanticipated transportation costs and delays;
- unfavorable weather conditions;
- hazards resulting from unusual or unexpected geological or environmental conditions;
- environmental regulations and requirements;
- accidental leakage of toxic or hazardous materials, such as petroleum liquids or drilling fluids, into the environment;
- changes in laws and regulations, including laws and regulations applicable to oil and natural gas activities or markets for the oil and natural gas produced;
- fluctuations in supply and demand for oil and natural gas causing variations of the prices we receive for our oil and natural gas production; and
- the availability of alternative fuels and the price at which they become available.

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We do not insure against all potential losses and could be materially and adversely affected by unexpected liabilities.

Our business is hazardous and is subject to all of the operating risks normally associated with the exploration, development, production, processing and transportation of oil, natural gas and NGLs. Such risks include potential blowouts, cratering, fires, loss of well control, mishandling of fluids and chemicals and possible underground migration of hydrocarbons and chemicals. The occurrence of any of these risks could result in environmental pollution, damage to or destruction of our property, equipment and natural resources, injury to person or loss of life. Additionally, for our non-operated properties, we generally depend on the operator for operational safety and regulatory compliance.

To mitigate financial losses resulting from these operational hazards, we maintain comprehensive general liability insurance, as well as insurance coverage against certain losses resulting from physical damages, loss of well control, business interruption and pollution events that are considered sudden and accidental. We also maintain worker's compensation and employer's liability insurance. However, our insurance coverage does not provide 100% reimbursement of potential losses resulting from these operational hazards. Additionally, insurance coverage is generally not available to us for pollution events that are considered gradual, and we have limited or no insurance coverage for certain risks such as political risk, war and terrorism. Our insurance does not cover penalties or fines assessed by governmental authorities. The occurrence of a significant event against which we are not fully insured could have a material adverse effect on our profitability, financial condition and liquidity.

Assets we acquire may prove to be worth less than we paid because of uncertainties in evaluating recoverable reserves and potential liabilities.

Our growth is primarily due to acquisitions of producing properties and underdeveloped leaseholds. We expect acquisitions may also contribute to our future growth. Successful acquisitions require an assessment of a number of factors, including estimates of recoverable reserves, exploration potential, future oil and natural gas prices, operating and capital costs and potential environmental and other liabilities. Such assessments are inexact and their accuracy is inherently uncertain. In connection with our assessments, we perform a review of the acquired properties which we believe is generally consistent with industry practices. However, such a review will not reveal all existing or potential problems. In addition, our review may not permit us to become sufficiently familiar with the properties to fully assess their deficiencies and capabilities. We do not inspect every well. Even when we inspect a well, we do not always discover structural, subsurface and environmental problems that may exist or arise in the future. We are generally not entitled to contractual indemnification for preclosing liabilities, including environmental liabilities. Normally, we acquire interests in properties on an "as is" basis with limited remedies for breaches of representations and warranties. Because of these factors, we may not be able to acquire oil and natural gas properties that contain economically recoverable reserves or be able to complete such acquisitions on acceptable terms.

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Title to the properties in which we have an interest may be impaired by title defects.

We generally conduct due diligence to review title on significant properties that we drill or acquire. However, there is no assurance that we will not suffer a monetary loss from title defects or title failure. Additionally, undeveloped acreage has greater risk of title defects than developed acreage. Generally, under the terms of the operating agreements affecting our properties, any monetary loss is due to title defects is to be borne by all parties to any such agreement in proportion to their interests in such property. If there are any title defects or defects in assignment of leasehold rights in properties in which we hold an interest, we will suffer a financial loss.

We depend on the skill, ability and decisions of third party operators to a significant extent.

The success of the drilling, development and production of the oil and natural gas properties in which we have or expect to have a non-operating working interest is substantially dependent upon the decisions of such third-party operators and their diligence to comply with various laws, rules and regulations affecting such properties. The failure of any third-party operator to make decisions, perform their services, discharge their obligations, deal with regulatory agencies, and comply with laws, rules and regulations, including environmental laws and regulations in a proper manner with respect to properties in which we have an interest could result in material adverse consequences to our interest in such properties, including substantial penalties and compliance costs. Such adverse consequences could result in substantial liabilities to us or reduce the value of our properties, which could negatively affect our results of operations.

We depend substantially on the continued presence of key personnel for critical management decisions and industry contacts.

Our success depends upon the continued contributions of our executive officers and key employees, particularly with respect to providing the critical management decisions and contacts necessary to manage and maintain growth within a highly competitive industry. Competition for qualified personnel can be intense, particularly in the oil and natural gas industry, and there are a limited number of people with the requisite knowledge and experience. Under these conditions, we could be unable to attract and retain these personnel. The loss of the services of any of our executive officers or other key employees for any reason could have a material adverse effect on our business, operating results, financial condition and cash flows.

Our operations in Israel may be adversely affected by economic and political developments.

We have interests in oil and gas leases and in oil and gas licenses in the waters off Israel. These interests are a significant portion of our future production and cash flow and may be adversely affected by political and economic developments, including the following:

- war, terrorist acts and civil disturbances,
- changes in taxation policies,
- laws and policies of the US and Israel affecting foreign investment, taxation, trade and business conduct,
- foreign exchange restrictions,
- international monetary fluctuations and changes in the value of the US dollar, such as the decline of the US dollar and

- other hazards arising out of Israeli governmental sovereignty over areas in which we own oil and gas interests.

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Members of Isramco's management team own a significant amount of common stock, giving them influence or control in corporate transactions and other matters, and the interests of these individuals could differ from those other shareholders.

Members of our management team beneficially own approximately 60.95% of our outstanding shares of common stock as of March 23, 2012. As a result, these shareholders are in a position to significantly influence or control the outcome of matters requiring a shareholder vote, including the election of directors, the adoption of an amendment to our certificate of incorporation or bylaws and the approval of mergers and other significant corporate transactions.

Our stock price is volatile and could continue to be volatile and has limited liquidity; Accordingly, investors may not be able to sell any significant number of shares of our stock at prevailing market prices.

Investor interest in our common stock may not lead to the development of an active or liquid trading market. The market price of our common stock has fluctuated in the past and is likely to continue to be volatile and subject to wide fluctuations. In addition, the stock market has experienced extreme price and volume fluctuations. The stock prices and trading volumes for our stock has fluctuated widely and the average daily trading volume of our stock continues to be limited and may continue for reasons that may be unrelated to business or results of operations. General economic, market and political conditions could also materially and adversely affect the market price of our common stock and investors may be unable to resell their shares of common stock at or above their purchase price. As a result of the limited trading in our stock, it may be difficult for investors to sell their shares in the public market at any given time at prevailing prices.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

Oil and Gas Exploration and Production - Properties and Reserves

Reserve Information. For estimates of Isramco's net proved reserves of natural gas, crude oil and natural gas liquids, see Note 16 to Consolidated Financial Statements, Supplemental Oil and Gas Information.

There are numerous uncertainties inherent in estimating quantities of proved reserves and in projecting future rates of production and timing of development expenditures, including many factors beyond the control of the producer. The reserve data set forth in Note 16 to Consolidated Financial Statements, Supplemental Oil and Gas Information, represent only estimates. Reserve engineering is a subjective process of estimating underground accumulations of natural gas, crude oil and condensate and natural gas liquids that cannot be measured in an exact manner. The accuracy of any reserve estimate is a function of the amount and quality of available data and of engineering and geological interpretation and judgment. As a result, estimates of different engineers normally vary. In addition, results of drilling, testing and production subsequent to the date of an estimate may justify revision of such estimate (upward or downward). Accordingly, reserve estimates are often different from the quantities ultimately recovered. The meaningfulness of such estimates is highly dependent upon the accuracy of the assumptions upon which they were based. For related discussion, see ITEM 1A. Risk Factors.

We believe that we have satisfactory title to the properties owned and used in our business, subject to liens for taxes not yet payable, liens incident to minor encumbrances, liens for credit arrangements and easements and restrictions that do not materially detract from the value of these properties, our interests in these properties, or the use of these properties in our business. We believe that our properties are adequate and suitable for us to conduct business in the

future.

ITEM 3. LEGAL PROCEEDINGS

We previously disclosed information relating to two putative shareholder derivative petitions that were filed by individual shareholders of the Company in the District Court of Harris County, Texas. These petitions each named certain of our officers and directors as defendants. Each of these suits claims that the shareholders were damaged as a result of various breaches of fiduciary duty, self dealing and other wrongdoing in connection with the Restated Agreement between the Company and Goodrich Global, Ltd (“Goodrich”) and other matters, primarily on the part of the Company’s Chairman and Chief Executive Officer, Haim Tsuff, and Jakob Maimon. Jakob Maimon is a former President and a director who resigned from all positions held with us on June 29, 2011.

On or about April 6, 2011, a third complaint was filed in the 295th District Court of Harris County, Texas by Yuval Ran, who claimed to be a shareholder, against certain of our officers and directors and several corporate parties controlled by Haim Tsuff. As with the prior suits, this complaint alleged various breaches of duty, self dealing and other wrongdoing in connection with the Restated Agreement between the Company and Goodrich, primarily on the part of the Company’s Chairman and Chief Executive Officer, Haim Tsuff, and Jakob Maimon. In addition, this suit alleged claims relating to other transactions between the Company and entities controlled by Haim Tsuff, including but not limited to the loan transactions between the Company and related parties, the lease and sale of a cruise ship, and the closure of the Company’s Israel branch office. The third complaint was transferred to the 55th Judicial District Court of Harris County, Texas, by order signed April 20, 2011, and consolidated with the above-referenced first and second complaints by order signed May 21, 2011, into a single case, called “Lead Cause No. 2010-34535; In Re Isramco, Inc. Shareholder Derivative Litigation; In the 55th Judicial District Court of Harris County, Texas (the “Derivative Litigation”).

We also disclosed information in our quarterly report for the three months ended September 30, 2011 relating to an additional putative shareholder derivative complaint that was filed by an individual shareholder, Yuval Lapiner, on July 7, 2011 in the Delaware Chancery Court in Wilmington, Delaware, naming certain of our officers and directors as defendants. The claims asserted in this case are essentially the same damage claims as asserted in the lawsuit filed in April 2011 and described above. The Company filed motions in the Chancery Court to Dismiss or Stay the lawsuit and, by order dated October 20, 2011, the case was dismissed. The plaintiff did not appeal. Yuval Lapiner then filed a motion to intervene in the Derivative Litigation and that motion was denied. Mr. Lapiner then filed a motion for attorney’s fees that was also denied. On December 12, 2011 the court approved the terms of the mediated settlement and entered final order and judgment in the case. The Company paid plaintiff attorney’s fees in the amount of \$1,000,000 and replaced its bylaws, amended various committee charters and adopted other corporate governance changes as set out in the stipulation. After the judgment was rendered Mr. Lapiner filed a motion for new trial and on February 12, 2012 filed a Notice of Appeal to the Fourteenth Court of Appeals in Houston, Texas. We do not believe the appeal will be successful nor do we believe there will be any change in the judgment.

On or about September 21, 2011, the Company’s former general counsel, Dennis Holifield resigned. Mr. Holifield had been hired in March, 2011. On or about October 12, 2011, Mr. Holifield submitted a “Summary Report” to the SEC (the “Summary Report”), in which made numerous factual allegations regarding Haim Tsuff, the Company’s Chief Executive Officer and Chairman; Edy Francis, the Company’s Chief Financial Officer; Amir Sanker, the Company’s Asset Manager; and other Company personnel. In the Summary Report, Mr. Holifield characterized the alleged conduct as illegal or criminal. On October 31, 2011 the Company received a written demand from, Mr. Holifield’s attorney on the Company for \$900,000.

Messrs. Tsuff, Francis, and Sanker have reviewed all of Mr. Holifield’s allegations and have advised the Company that they have not engaged in any criminal conduct or other illegal activity. As of November 3, 2011, the Company’s Board of Directors has constituted a committee of independent directors consisting of Max Pridgeon and Asaf Yarkoni which has been directed to investigate all of the Holifield allegations and report back to the full board and make any

recommendations, if any, for corrective action.

From time to time, we are involved in disputes and other legal actions arising in the ordinary course of business. In management's opinion, none of these other disputes and legal actions is expected to have a material impact on our consolidated financial position or results of operations.

ITEM 4.

Not applicable.

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PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

Our common stock is listed on the Nasdaq Capital Market under the symbol "ISRL". The following table sets forth for the periods indicated, the reported high and low closing prices for our common stock . As of March 22, 2012, there were approximately 268 holders of record of our common stock.

	High	Low
2011		
First Quarter	\$ 86.50	\$ 56.14
Second Quarter	68.66	58.99
Third Quarter	69.00	53.40
Fourth Quarter	93.40	55.05
2010		
First Quarter	\$ 80.10	\$ 49.00
Second Quarter	70.50	45.05
Third Quarter	61.12	45.56
Fourth Quarter	90.36	55.96

We have never paid cash dividends on our common stock. We intend to retain earnings for use in the operation and expansion of our business and therefore do not anticipate declaring cash dividends on our common stock in the foreseeable future. Any future determination to pay dividends on common stock will be at the discretion of the board of directors and will be dependent upon then existing conditions, including other factors, as the board of directors deems relevant.

ITEM 6. SELECTED FINANCIAL DATA

Not applicable

ITEM 7. MANAGEMENT DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

THE FOLLOWING COMMENTARY SHOULD BE READ IN CONJUNCTION WITH THE CONSOLIDATED FINANCIAL STATEMENTS AND RELATED NOTES CONTAINED ELSEWHERE IN THIS FORM 10-K. THE DISCUSSION CONTAINS FORWARD-LOOKING STATEMENTS THAT INVOLVE RISKS AND UNCERTAINTIES. THESE STATEMENTS RELATE TO FUTURE EVENTS OR OUR FUTURE FINANCIAL PERFORMANCE. IN SOME CASES, YOU CAN IDENTIFY THESE FORWARD-LOOKING STATEMENTS BY TERMINOLOGY SUCH AS "MAY," "WILL," "SHOULD," "EXPECT," "PLAN," "ANTICIPATE," "BELIEVE," "ESTIMATE," "PREDICT," "POTENTIAL," "INTEND," OR "CONTINUE," AND SIMILAR EXPRESSIONS. THESE STATEMENTS ARE ONLY PREDICTIONS. OUR ACTUAL RESULTS MAY DIFFER MATERIALLY FROM THOSE ANTICIPATED IN THESE FORWARD-LOOKING STATEMENTS AS A RESULT OF A VARIETY OF FACTORS, INCLUDING, BUT NOT LIMITED TO, THOSE SET FORTH UNDER "RISK FACTORS" AND ELSEWHERE IN THIS FORM 10-K.

Overview

We are an independent oil and natural gas company engaged in the exploration, development and production of oil and natural gas properties located onshore in the United States and an owner of various royalty interests offshore Israel. Our properties are primarily located in Texas, New Mexico and Oklahoma and Israel. We act as the operator of most of our U.S. properties. Historically, we have grown through acquisitions, with a focus on properties within our core operating areas that we believe have significant development and exploration opportunities and where we can apply our technical experience and economies of scale to increase production and proved reserves while lowering lease operating costs. In 2011 we created a new subsidiary that provides well maintenance and workover services, well completion and recompletion services.

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Our financial results depend upon many factors, but are largely driven by the volume of our oil and natural gas production and the price that we receive for that production. Our production volumes will decline as reserves are depleted unless we expend capital in successful development and exploration activities or acquire additional properties with existing production. The amount we realize for our production depends predominantly upon commodity prices, which are affected by changes in market demand and supply, as impacted by overall economic activity, weather, pipeline capacity constraints, inventory storage levels, basis differentials and other factors, and secondarily upon our commodity price hedging activities. Accordingly, finding and developing oil and natural gas reserves at economical costs is critical to our long-term success. Our future drilling plans are subject to change based upon various factors, some of which are beyond our control, including drilling results, oil and natural gas prices, the availability and cost of capital, drilling and production costs, availability of drilling services and equipment, gathering system and pipeline transportation constraints and regulatory approvals. To the extent these factors lead to reductions in our drilling plans and associated capital budgets in future periods, our financial position, cash flows and operating results could be adversely impacted.

At December 31, 2011, our estimated total proved oil, natural gas reserves and natural gas liquids, as prepared by our independent reserve engineering firms, Netherland, Sewell & Associates, Inc and Cawley, Gillespie & Associates, Inc., were approximately 34,990 thousand barrels of oil equivalent (“MBOE”), consisting of 3,234 thousand barrels (MBbls) of oil, and 179,155 million cubic feet (MMcf) of natural gas and 1,896 thousand barrels (MBbls) of natural gas liquids. Approximately 27% of our proved reserves were classified as proved developed (See Note 16 Supplemental Oil and Gas Information to Consolidated Financial Statements to our consolidated financial statements). Full year 2011 production averaged 2.16 MBOE/d compared to 2.3 MBOE/d in 2010.

Critical accounting policies

The discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of our consolidated financial statements requires us to make estimates and assumptions that affect our reported results of operations and the amount of reported assets, liabilities and proved oil and natural gas reserves. Some accounting policies involve judgments and uncertainties to such an extent that there is reasonable likelihood that materially different amounts could have been reported under different conditions, or if different assumptions had been used. Actual results may differ from the estimates and assumptions used in the preparation of our consolidated financial statements. Described below are the most significant policies we apply in preparing our consolidated financial statements, some of which are subject to alternative treatments under accounting principles generally accepted in the United States. We also describe the most significant estimates and assumptions we make in applying these policies.

Oil and Natural Gas Activities

Accounting for oil and natural gas activities is subject to unique rules. Two generally accepted methods of accounting for oil and natural gas activities are available - successful efforts and full cost. The most significant differences between these two methods are the treatment of unsuccessful exploration costs and the manner in which the carrying value of oil and natural gas properties are amortized and evaluated for impairment. The successful efforts method requires unsuccessful exploration costs to be expensed as they are incurred upon a determination that the well is uneconomical, while the full cost method provides for the capitalization of these costs. Both methods generally provide for the periodic amortization of capitalized costs based on proved reserve quantities. Impairment of oil and natural gas properties under the successful efforts method is based on an evaluation of the carrying value of individual oil and natural gas properties against their estimated fair value, while impairment under the full cost method requires an evaluation of the carrying value of oil and natural gas properties included in a cost center against the net present value of future cash flows from the related proved reserves, using period-end prices and costs and a 10% discount rate.

We account for our natural gas and crude oil exploration and production activities under the successful efforts method of accounting.

Proved Oil and Natural Gas Reserves

Isramco estimates its proved oil and gas reserves as defined by the SEC and the FASB. This definition includes crude oil, natural gas, and NGLs that geological and engineering data demonstrate with reasonable certainty to be economically producible in future periods from known reservoirs under existing economic conditions, operating methods, government regulations, etc., i.e., at prices and costs as of the date the estimates are made. Prices include consideration of price changes provided only by contractual arrangements, and do not include adjustments based upon expected future conditions.

The Company's estimates of proved reserves are made using available geological and reservoir data, as well as production performance data. These estimates are reviewed annually by our independent reserve engineering firm, Cawley, Gillespie & Associates, Inc and revised, either upward or downward, as warranted by additional data. Revisions are necessary due to changes in, among other things, reservoir performance, prices, economic conditions, and governmental restrictions, as well as changes in the expected recovery associated with infill drilling. Decreases in prices, for example, may cause a reduction in some proved reserves due to reaching economic limits earlier. A material adverse change in the estimated volumes of proved reserves could have a negative impact on DD&A and could result in property impairments.

Depreciation, Depletion and Amortization

Our rate of recording depreciation, depletion and amortization expense (DD&A) is primarily dependent upon our estimate of proved reserves, which is utilized in our unit-of-production method calculation. If the estimates of proved reserves were to be reduced, the rate at which we record DD&A expense would increase, reducing net income. Such a reduction in reserves may result from lower market prices, which may make it non-economic to drill for and produce higher cost reserves.

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Impairment

We review our property and equipment in accordance with Accounting Standards Codification (ASC) 360, Property, Plant, and Equipment (ASC 360). ASC 360 requires us to evaluate property and equipment as an event occurs or circumstances change that would more likely than not reduce the fair value of the property and equipment below the carrying amount. If the carrying amount of property and equipment is not recoverable from its undiscounted cash flows, then we would recognize an impairment loss for the difference between the carrying amount and the current fair value. Further, we evaluate the remaining useful lives of property and equipment at each reporting period to determine whether events and circumstances warrant a revision to the remaining depreciation periods.

Asset Retirement Obligations

We have significant obligations to remove tangible equipment and facilities associated with our oil and gas wells and to restore land at the end of oil and gas production operations. Our removal and restoration obligations are most often associated with plugging and abandoning wells. Estimating the future restoration and removal costs is difficult and requires us to make estimates and judgments because most of the removal obligations we have will be take effect in the future. Additionally, these operations are subject to private contracts and government regulations that often have vague descriptions of what is required. Asset removal technologies and costs are constantly changing, as are regulatory, political, environmental, safety and public relations considerations. Inherent in the present value calculations are numerous assumptions and judgments including the ultimate removal cost amounts, inflation factors, credit adjusted discount rates, timing of obligations and changes in the legal, regulatory, environmental and political environments.

Accounting for Derivative Instruments and Hedging Activities

We utilize derivative contracts to hedge against the variability in cash flows associated with the forecasted sale of our anticipated future oil and natural gas production. We generally hedge a substantial, but varying, portion of our anticipated oil and natural gas production for the next 36 and 3 months, respectively. We do not use derivative instruments for trading purposes. We have elected not to apply hedge accounting to our derivative contracts, which would potentially allow us to not record the change in fair value of our derivative contracts in the consolidated statements of operations. We carry our derivatives at fair value on our consolidated balance sheets, with the changes in the fair value included in our consolidated statements of operations in the period in which the change occurs. Our results of operations would potentially have been significantly different had we elected and qualified for hedge accounting on our derivative contracts.

Environmental Obligations and Other Contingencies

Management makes judgments and estimates in accordance with applicable accounting rules when it establishes reserves for environmental remediation, litigation, and other contingent matters. Provisions for such matters are charged to expense when it is probable that a liability is incurred and reasonable estimates of the liability can be made. Estimates of environmental liabilities are based on a variety of matters, including, but not limited to, the stage of investigation, the stage of the remedial design, evaluation of existing remediation technologies, and presently enacted laws and regulations. In future periods, a number of factors could significantly change the Company's estimate of environmental-remediation costs, such as changes in laws and regulations, changes in the interpretation or administration of laws and regulations, revisions to the remedial design, unanticipated construction problems, identification of additional areas or volumes of contaminated soil and groundwater, and changes in costs of labor, equipment, and technology. Consequently, it is not possible for management to reliably estimate the amount and timing of all future expenditures related to environmental or other contingent matters and actual costs may vary significantly from the Company's estimates. The Company's in-house legal counsel regularly assesses these contingent

liabilities and, in certain circumstances, consults with third-party legal counsel or consultants to assist in forming the Company's conclusion.

Income Taxes

The Company follows ASC 740, Income Taxes, (ASC 740), which requires recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been included in the consolidated financial statements or tax returns. Under this method, deferred tax assets and liabilities are computed using the liability method based on the differences between the financial statement and tax basis of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse.

A valuation allowance is provided, if necessary, to reserve the amount of net operating loss and net deferred tax assets which the Company may not be able to use because of the expiration of maximum carryover periods allowed under applicable tax codes.

Liquidity and Capital Resources

Our primary historical sources of capital and liquidity are internally generated cash flows from operations, availability under our senior credit agreement with our unrelated bank lenders with Bank of Nova Scotia ("Senior Credit Agreements") and loans from various related party lenders ("Related Party Loans") and asset dispositions. We continuously monitor our liquidity and evaluate our development plans in light of a variety of factors, including, but not limited to, our cash flows, capital resources and drilling success.

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Note 6 to our Consolidated Financial Statements, Long-Term Debt and Interest Expense, describes the Senior Credit Agreements and Related Party Loans. Our Senior Credit Agreements originally provided a total \$300 million in credit facilities. As of December 31, 2011, the total available borrowing base was zero.

On March 3, 2011 the Company terminated its relationship with Wells Fargo and repaid its outstanding balance.

The borrowing base which relates to our oil and natural gas properties is redetermined on a semi-annual basis (with the Company and the lenders each having the right to one unscheduled redetermination per year) and adjusted based on our oil and natural gas properties, reserves, other indebtedness and other relevant factors. During the fourth quarter of 2011 the Lenders reduced the borrowing base to \$0. The Company is repaying the approximately \$20,000,000 outstanding balance in six installments of \$3,333,000 each with the first two payments already made for January and February 2012 and the remaining installments due each month thereafter through June 2012 when the entire balance will be repaid. The Company is also in negotiations for similar credit facilities with several other commercial lenders, to obtain terms most favorable to the Company. While optimistic of a positive outcome of our consolidation efforts, the Company is uncertain as to whether it will be successful in obtaining new replacement financing or, if it is obtained, the timetable upon which such facility will be closed and other material terms and conditions. The Company believes that during the interim period that the terms of existing affiliate financing will remain flexible and additional funding will be made available if needed until a new credit facility can be entered. See Note 6 to Consolidated Financial Statements, Long-Term Debt and Interest Expense.

Our future capital resources and liquidity may depend, in part, on our success in developing the leasehold interests that we have acquired. Cash is required to fund capital expenditures necessary to offset inherent declines in production and proven reserves, which is typical in the capital-intensive oil and gas industry. Future success in growing reserves and production will be highly dependent on capital resources available and the success in finding and acquiring additional reserves. We expect to fund our future capital requirements through internally generated cash flows and borrowings under our Senior Credit Agreements. Long-term cash flows are subject to a number of variables, including the level of production and prices and our commodity price hedging activities as well as various economic conditions that have historically affected the oil and natural gas industry.

Debt

	2011	As of December 31,	
		2010	2009
		(In thousands except percentage)	
Senior Credit Facilities	\$ -	\$ 22,725	\$ 32,950
Long – term debt – related party	60,211	76,354	79,354
Short – term debt – related party	6,456	-	-
Current maturities of long-term debt, short-term debt and bank overdraft	32,009	17,350	12,366
Total debt	98,676	116,429	124,670
Stockholders' equity	18,548	18,537	13,733
Debt to capital ratio	84%	86%	90%

At year-end 2011, our total debt was \$98,676,000, compared to total debt of \$116,429,000 at year-end 2010 and \$124,670,000 at year-end 2009. As of December 31, 2011, current debt included \$20,000,000 as current maturities of the Senior Credit Facilities. During the fourth quarter of 2011 the Lenders reduced the borrowing base to \$0. The Company is repaying the approximately \$20,000,000 outstanding balance in six installments of \$3,333,000 each with the first two payments already made for January and February 2012 and the remaining installments due each month thereafter through June 2012 when the entire balance will be repaid.

On March 3, 2011, the Company entered into a Loan Agreement with I. O. C. - Israel Oil Company, LTD., an affiliate of the Company ("IOC") pursuant to which it borrowed the sum of \$11 million. The loan bears interest at a rate of 10% per annum and is payable in quarterly payments of interest only until March 3, 2012, when all accrued interest and principal is due and payable. The loan may be prepaid at any time without penalty. The loan is unsecured. The purpose of the loan was to provide funds to Isramco for the payment of amounts due under the Wells Fargo Senior Credit Facility at maturity. On March 3, 2011 Isramco paid the outstanding principal balance due under the Wells Fargo Senior Credit Agreement. Subsequently, on March 9, 2011, pursuant to an agreement with Wells Fargo, the derivative contracts between Isramco and Wells Fargo were terminated at a cost to the Company of approximately \$7,000,000. Concurrently, the Company entered into new derivative contracts for 336,780 barrels of crude oil during the 46 month period commencing March 2011 with Macquarie Bank, N.A. During September 2011 Isramco paid \$5,096,000 of principal and interest pursuant to Loan agreement with IOC. The Company is actively pursuing a consolidation of all outstanding debt with Macquarie Bank and other commercial lenders.

In October 2011 the agreement with IOC, pertaining to a loan in the outstanding principal amount of \$6,456,000 was renegotiated. The payoff of principal amount was extended by 6 months to September 9, 2012. Interest accrued per annum was determined on LIBOR+5.5% from initial 10%.

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Off-Balance Sheet Arrangements

At December 31, 2011, we did not have any off-balance sheet arrangements.

Cash Flow

Our primary source of cash in 2011 was cash flow from operating activities, loans from related party and proceeds from sale of investment in MediaMind Ltd shares. Our primary source of cash in 2010 and 2009 was our operating activities. In 2011 cash received from operations, from selling of investment in MediaMind Ltd shares and from related party was offset by repayments of borrowings under our Senior Credit Agreements, repayment of related party loans, purchase of equipment and payments made on settled derivatives contracts. In 2010 and 2009, cash received from operations was offset by repayments of borrowings under our Senior Credit Agreements and cash used in payments on addition to oil and gas properties, net of any divestiture activities.

Operating cash flow fluctuations were substantially driven by changes in commodity prices and changes in our production volumes. Working capital was substantially influenced by these variables. Fluctuation in commodity prices and our overall cash flow may result in an increase or decrease in our future capital expenditures. Prices for oil and natural gas have historically been subject to seasonal fluctuations characterized by peak demand and higher prices in the winter heating season; however, the impact of other risks and uncertainties have influenced prices throughout recent years. See Results of Operations below for a review of the impact of prices and volumes on sales.

	Years Ended December 31,		
	2011	2010	2009
	(In thousands)		
Cash flows provided by operating activities	\$ 6,946	\$ 12,063	\$ 21,519
Cash flows provided by (used in) investing activities	7,643	(1,437)	(332)
Cash flows used in financing activities	(18,124)	(7,876)	(21,421)
Net increase (decrease) in cash	\$ (3,535)	\$ 2,750	\$ (234)

Operating Activities, Net cash flows provided by operating activities were \$6,946,000, \$12,063,000 and \$21,519,000 for the years ended December 31, 2011, 2010 and 2009, respectively. Key drivers of net operating cash flows are commodity prices, production volumes, hedging activities and operating cost.

During the year ended December 31, 2011, compared to the same period in 2010, net cash flow provided by operating activities decreased by \$5,117,000 to \$6,946,000. This decrease was primarily attributable to net cash paid on settled derivatives contracts of \$7,007,000, less cash received on proceeds from settlements of derivative contracts, higher lease operating expenses all of which were partially offset by increased oil and natural gas liquids (“NGLs”) revenues. The increase in revenues was primarily attributable to higher average oil and NGLs prices for the year ended December 31, 2011 of \$94.12/bbl and \$50.24/bbl respectively, compared to \$77.26/bbl and \$36.97/bbl for the year ended December 31, 2010. However, we are unable to predict future production levels or future commodity prices, and, therefore, we cannot predict future levels of net cash provided by operating activities.

Net cash provided by operating activities decreased in 2010 compared to 2009 primarily due to a reduction in working capital of \$4,549,000, higher lease operating expenses and expenses related to our well plugging and abandonment obligations. The reduction in net cash proceeds from our commodity price hedging activities of \$8,308,000 was offset

by increased oil and natural gas revenues of \$8,561,000. The increase in revenues was primarily attributable to higher average oil, gas and NGLs prices for the year ended December 31, 2010 of \$77.26/bbl, \$4.71/mcf and \$36.97/bbl, compared to \$58.52/bbl, \$3.48/mcf and \$28.83/bbl for the year ended December 31, 2009.

Investing Activities, The primary driver of cash provided by investing activities in 2011 was proceeds from sale of marketable securities which was offset by purchase of other property and equipment of approximately \$6,500,000 and an additional \$2,549,000 spent on capital expenditures. Net cash flows provided (used in) in investing activities for the years ended December 31, 2011 and 2010 were \$7,643,000 and \$(1,437,000) respectively.

In 2010, we spent an additional \$3,454,000 on capital expenditures and an additional \$157,000 on other property and equipment. We participated in the drilling of 3 gross wells in 2010. In December, 2010, we completed the sale of our interests in certain properties in Wise and Parker Counties, Texas, for approximately \$2.2 million.

In 2009, we spent an additional \$645,000 on capital expenditures and other property and equipment.

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Financing Activities, Net cash flows used in financing activities were \$18,124,000 and \$7,876,000 for the years ended December 31, 2011 and 2010, respectively. Excess cash flow from proceeds of sale of marketable securities, operations and a loan from related party were primarily used to repay borrowings under our Senior Credit Agreements to the extent available. During the year ended in 2011, we repaid borrowings of \$29,612,000. During the year ended in 2010, we repaid borrowings of \$7,876,000.

Results of Continuing Operations

	Selected Data		
	Years Ended December 31,		
	2011	2010	2009
	(In thousands except per share and MBOE amounts)		
Financial Results			
Oil and Gas sales	\$ 44,228	\$ 39,329	\$ 30,768
Other	1,420	2,871	956
Total revenues and other	45,648	42,200	31,724
Cost and expenses	41,278	41,059	42,024
Other expense (income)	(6,991)	5,784	13,369
Income tax expense (benefit)	3,975	(1,856)	(10,090)
Net income (loss) attributable to common shareholders	7,386	(2,787)	(13,579)
Net income attributable to noncontrolling interests	5	-	-
Net income (loss) attributable to Isramco	7,381	(2,787)	(13,579)
Earnings (loss) per common share – basic	\$ 2.72	\$ (1.03)	\$ (5.00)
Earnings (loss) per common share –diluted	\$ 2.72	\$ (1.03)	\$ (5.00)
Weighted average number of shares outstanding-basic	2,717,691	2,717,691	2,717,691
Weighted average number of shares outstanding- diluted	2,717,691	2,717,691	2,717,691
Operating Results			
Adjusted EBITDAX (1)	\$ 30,606	\$ 22,472	\$ 26,796
Total proved reserves (MBOE)	34,990	9,031	8,565
Annual sales volumes (MBOE)	789	841	886

Average cost per
MBOE:

Production (excluding transportation and taxes)	\$	20.55	\$	18.32	\$	12.99
General and administrative	\$	5.63	\$	6.09	\$	4.64
Depletion	\$	12.66	\$	14.44	\$	17.34

- (1) See Adjusted EBITDAX for a description of Adjusted EBITDAX, which is not a Generally Accepted Accounting Principles (GAAP) measure, and a reconciliation of Adjusted EBITDAX to income from operations before income taxes, which is presented in accordance with GAAP.

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Financial Results

Net Income, our net income was \$7,381,000, or \$2.72 per share for the year ended December 31, 2011. This compares to net loss of (\$2,787,000), or (\$1.03) per share, for the year ended December 31, 2010.

The increase in net income was primarily due to the impact of sale of marketable securities, derivatives, higher oil and NGLs sales revenues due to higher prices and lower depreciation, depletion and amortization expenses. This was partially offset by a decrease in sales volumes of natural gas, oil and natural gas liquids (“NGLs”) caused by natural decline in production, higher taxes paid due to increase in revenues, higher impairments of oil and gas assets and higher lease operating expenses.

Our net loss for 2010 totaled (\$2,787,000), or (\$1.03) per share, compared to a net loss for 2009 of (\$13,579,000), or (\$5.00) per share. The decrease in net loss was primarily due to higher natural gas, oil and NGLs sales revenues due to higher prices, the impact of derivatives, lower depreciation, depletion and amortization expenses and lower interest expense. This was partially offset by a decrease in sales volumes of natural gas, oil and NGLs caused by adverse weather conditions in Texas that restricted our ability to access, repair and maintain our wells in the first quarter of 2010, along with the natural decline in production, and higher lease operating expenses.

Revenues, Volumes and Average Prices

Sales Revenues

In thousands except percentages	Years Ended December 31,					
	2011	2010	D vs. 2011	2009	D vs. 2010	
Gas sales	\$ 11,135	\$ 11,157	NM%	\$ 9,124	22%	
Oil sales	26,260	22,405	17	17,147	31	
Natural gas liquid sales	6,833	5,767	18	4,497	28	
Total	\$ 44,228	\$ 39,329	12%	\$ 30,768	28%	

NM—not meaningful

Our sales revenues for the year ended December 31, 2011 increased by 12% when compared to the same period of 2010, mainly due to higher oil and NGLs commodity prices. Our sales revenues for the year ended December 31, 2010 increased by 28% when compared to the same period of 2009, mainly due to higher natural gas, oil and condensate and NGLs commodity prices.

Volumes and Average Prices

	Years Ended December 31,					
	2011	2010	D vs. 2011	2009	D vs. 2010	
Natural Gas						
Sales volumes Mmcf (2)	2,241	2,368	(5)%	2,623	(10)%	
Price per Mcf (1)	\$ 4.97	\$ 4.71	6	\$ 3.48	35	
Total gas sales revenues (thousands)	\$ 11,135	\$ 11,157	NM	\$ 9,124	22%	
Crude Oil						
Sales volumes MBbl	279	290	(4)%	293	(1)%	
Price per Bbl (1)	\$ 94.12	\$ 77.26	22	\$ 58.52	32	
	\$ 26,260	\$ 22,405	17%	\$ 17,147	31%	

Total oil sales revenues
(thousands)

Natural gas liquids

Sales volumes MBbl (2)	136	156	(13)%	156	NM%
Price per Bbl (1)	\$ 50.24	\$ 36.97	36	\$ 28.83	28
Total natural gas liquids sales revenues (thousands)	\$ 6,833	\$ 5,767	18%	\$ 4,497	28%

- (1) Amounts exclude the impact of cash paid/received on settled contracts as we did not elect to apply hedge accounting.
- (2) At the end of 2010, the company sold interests in several oil and gas properties which resulted in lower natural gas, oil and natural gas liquids ("NGLs") volumes in 2011.

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The company's natural gas sales volumes decreased by 5%, crude oil sales volumes by 4% and natural gas liquids sales volumes by 13% for the year ended December 31, 2011 compared to the same period of 2010. This decrease was primarily caused by natural decline in production.

Our average natural gas price for the year ended December 31, 2011 increased by 6%, or \$0.26 per Mcf, when compared to the same period of 2010. Our average crude oil price for the year ended December 31, 2011 increased by 22%, or \$16.86 per Bbl, when compared to the same period of 2010. Our average natural gas liquids price for the ended December 31, 2011 increased by 36%, or \$13.27 per Bbl, when compared to the same period of 2010.

In 2010 the Company's natural gas sale volumes decreased by 10%, crude oil sale volumes by 1% and natural gas liquid sale volumes by 0% compared to 2009. This decrease was primarily caused by adverse weather conditions in Texas that restricted our ability to access, repair and maintain our wells in the first quarter of 2010, along with the natural decline in production.

Analysis of Oil and Gas Operations Sales Revenues

The following table provides a summary of the effects of changes in volumes and prices on Isramco's sales revenues for the year ended December 31, 2011 compared to 2010 and 2009.

In thousands	Natural Gas	Oil	Natural gas liquids
2009 sales revenues	\$ 9,124	\$ 17,147	\$ 4,497
Changes associated with sales volumes	(887)	(176)	-
Changes in prices	2,920	5,434	1,270
2010 sales revenues	11,157	22,405	5,767
Changes associated with sales volumes	(598)	(850)	(739)
Changes in prices	576	4,705	1,805
2011 sales revenues	\$ 11,135	\$ 26,260	\$ 6,833

Adjusted EBITDAX.

To assess the operating results of Isramco, management analyzes income from operations before income taxes, interest expense, exploration expense, unrealized gain (loss) on derivative contracts and DD&A expense and impairments ("Adjusted EBITDAX"). Adjusted EBITDAX is not a GAAP measure. Isramco's definition of Adjusted EBITDAX excludes exploration expense because exploration expense is not an indicator of operating efficiency for a given reporting period, but rather is monitored by management as a part of the costs incurred in exploration and development activities. Similarly, Isramco excludes DD&A expense and impairments from Adjusted EBITDAX as a measure of segment operating performance because capital expenditures are evaluated at the time capital costs are incurred. The Company's definition of Adjusted EBITDAX also excludes interest expense to allow for assessment of segment operating results without regard to Isramco's financing methods or capital structure. Adjusted EBITDAX is a widely accepted financial indicator of a company's ability to incur and service debt, fund capital expenditures and make payments on its long term loans. Management believes that the presentation of Adjusted EBITDAX provides information useful in assessing the Company's financial condition and results of operations.

However, Adjusted EBITDAX, as defined by Isramco, may not be comparable to similarly titled measures used by other companies. Therefore, Isramco's consolidated Adjusted EBITDAX should be considered in conjunction with income (loss) from operations and other performance measures prepared in accordance with GAAP, such as operating

income or cash flow from operating activities. Adjusted EBITDAX has important limitations as an analytical tool because it excludes certain items that affect income from continuing operations and net cash provided by operating activities. Adjusted EBITDAX should not be considered in isolation or as a substitute for an analysis of Isramco's results as reported under GAAP. Below is a reconciliation of consolidated Adjusted EBITDAX to income (loss) from operations before income taxes.

In thousands	Years Ended December 31,		
	2011	2010	2009
Income from operations before income taxes	\$ 11,361	\$ (4,643)	\$ (23,669)
Depreciation, depletion, amortization and impairment expense	14,016	13,893	21,119
Interest expense	7,760	7,646	9,219
Unrealized gain on derivative contract	(3,384)	4,727	19,298
Accretion Expenses	853	849	829
Consolidated Adjusted EBITDAX	\$ 30,606	\$ 22,472	\$ 26,796

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Operating Expenses

In thousands except percentages	Years Ended December 31,				
	2011	2010	D vs. 2011	2009	D vs. 2010
Lease operating expense, transportation and taxes	\$ 20,981	\$ 19,894	5%	\$ 15,651	27%
Depreciation, depletion and amortization	9,982	12,142	(18)	15,368	(21)
Impairments of oil and gas assets	4,034	1,751	130	5,751	(70)
Accretion expense	853	849	NM	829	2
Production Services	675	-	-	-	-
Loss from plug and abandonment	315	1,300	(76)	312	317
General and administrative	4,438	5,123	(13)	4,113	25
	\$ 41,278	\$ 41,059	1%	\$ 42,024	(2)%

During 2011, our operating expenses increased by 1% when compared to 2010 due to the following factors:

- Lease operating expense, transportation cost and taxes increased by 5%, or \$1,087,000 in 2011 when compared to 2010. This increase was the result of the costs associated with a plan we initiated last year to workover a number of our wells, along with the incremental costs involved in operating older, more mature fields that require additional repair and maintenance. In addition due to changes in regulatory requirements in Texas we incurred additional expenses regarding previously inactive wells in order to renew production in the future. Finally, the higher oil and NGL sales increased the taxes paid during 2011. On a per unit basis, lease operating expenses (excluding transportation and taxes) increased by \$2.23 per MBOE to \$20.55 per MBOE in 2011 from \$18.32 per MBOE in 2010.
- Depreciation, Depletion & Amortization (DD&A) of the cost of proved oil and gas properties is calculated using the unit-of-production method. Our DD&A rate and expense are the composite of numerous individual field calculations. There are several factors that can impact our composite DD&A rate and expe