FELLOWS ENERGY LTD
Form 10QSB/A
February 13, 2006

United States
Securities And Exchange Commission
Washington, D.C. 20549

Amendment No. 2
to
Form 10-QSB/A

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

FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2005

Commission File Number: 000-33321

Fellows Energy Ltd.
(Exact Name of Small Business Issuer as Specified in its Charter)

Nevada	**33-0967648**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

370 Interlocken Boulevard, Suite 400
Broomfield, Colorado 80021

(Address of Principal Executive Offices)

(303) 327-1525
(Registrant's Telephone Number, Including Area Code)

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. x Yes ¨ No

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes [ ] No [x]

State the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date: As of November 8, 2005 there were 47,878,806 shares of the issuer's $.001 par value common stock issued and

outstanding.

Transitional Small Business Disclosure Format: ¨ Yes x No

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FELLOWS ENERGY LTD.
(A Development Stage Company)

Quarterly Report on Form 10-QSB for the
Quarterly Period Ending September 30, 2005

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Explanatory Note

This amended quarterly report on Form 10-QSB/A is filed to add inception-to-date (from November 12, 2003 to September 30, 2005) numbers in accordance SFAS 7, as well as include our audited balance sheet as of December 31, 2004, to comply with the Rule 10-01(c)(1) of Regulation S-X. Additionally, this amended quarterly report is filed to properly value the assets acquired during the exchange of oil and gas interests from Diamond Oil and Gas and the $3.5 million of common stock issued.

Part I: Financial Information
Item 1. Financial Statements

Fellows Energy Ltd.
(A Development Stage Company)
Balance Sheet
(Unaudited)

		September 30, 2005	December 31, 2004
Assets			
Cash and Cash Equivalents	$	2,560,489	149,027
Marketable securities, available-for-sale		364,347	—
Accounts Receivable		1,976	—
Interest Receivable		179	—
Prepaid Expenses		15,000	—
Total current assets		2,941,991	149,027
Unproved oil & gas property		10,618,072	9,043,648
Equipment, net of $12,014 and $1,100 accumulated depreciation respectively		52,321	16,563
Deposits		475,500	—
Restricted cash		235,000	135,000
Deferred debt issue costs		610,022	—
Total assets	$	14,932,906	9,344,238
Liabilities And Stockholders' Equity			
Accounts payable	$	341,474	434,411
Notes payable		—	1,556,379
Total current liabilities		341,474	1,990,790
Convertible note payable		—	350,000
Convertible debenture		6,145,599	1,000,000
Stockholders' equity:			
Preferred stock, $.001 par value; 25,000,000 shares authorized; none outstanding		—	—
Common stock, $.001 par value; 100,000,000 shares authorized; 47,878,806 shares issued and outstanding		47,878	41,743
Additional paid-in capital		13,335,602	9,556,702
Stock issuance obligation		—	362,500
Accumulated deficit		(197,189)	(197,189)
Deficit accumulated during the development stage		(4,742,089)	(3,760,308)
Accumulated other comprehensive income		1,631	—
Total stockholders' equity		8,445,833	6,003,448
Total liabilities and stockholders' equity	$	14,932,906	9,344,238

See accompanying notes to financial statements

Fellows Energy Ltd.
(A Development Stage Company)

Statements of Operations
(Unaudited)

	Nine Months Ended September 30, 2005	Nine Months Ended September 30, 2004	Three Months Ended September 30, 2005	Three Months Ended September 30, 2004	Inception (Nov. 12, 2003) to September 30, 2005
Revenue	$ —	$ —	$ —	$ —	$ —
Operating expense					
Exploration	904,400	120,591	640,507	57,357	3,157,695
General and administrative	1,770,587	472,944	812,909	198,626	3,141,867
Operating (loss)	(2,674,987)	(593,535)	(1,453,416)	(255,983)	(6,299,562)
Other income (expense)					
Interest expense	(176,816)	(56,518)	(47,501)	(34,989)	(312,549)
Gain on Sale of Property	1,442,674	—	—	—	1,442,674
Gain on extinguishment of debt	383,531	—	—	—	383,531
Miscellaneous	(3,208)	—	(2,445)	—	(3,076)
Total other income (expense)	1,646,313	(56,518)	(49,946)	(34,989)	1,510,580
Loss before income tax	(1,028,674)	(650,053)	(1,503,362)	(290,972)	(4,788,982)
Income tax expense	—	—	—	—	—
Deferred tax benefit	—	—	—	—	—
Net Loss	$ (1,028,674)	$ (650,053)	$ (1,503,362)	$ (290,972)	$ (4,788,982)
Other comprehensive income (loss)					
Realized gain on sale of marketable securities	132	—	132	—	132
Unrealized holding gains on marketable securities	1,499	—	1,499	—	1,499
Comprehensive Loss	$ (1,027,175)	(650,053)	$ (1,501,731)	(290,972)	$ (4,787,351)
Basic earnings (loss) per share	$ (0.02)	$ (0.02)	$ (0.03)	$ (0.01)	$ (0.11)
Basic weighted average shares outstanding	45,632,281	42,169,938	47,878,806	41,493,150	43,593,835
Diluted earnings (loss) per share	(0.01)	(0.02)	(0.02)	(0.01)	(0.9)
	71,700,527	42,169,938	73,947,052	41,493,150	54,765,940

Diluted weighted average shares outstanding	

See accompanying notes to financial statements

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Fellows Energy Ltd.
(A Development Stage Company)

Cash Flow Statement
(Unaudited)

	Nine Months Ended September 30, 2005	Nine Months Ended September 30, 2004	Inception (Nov 12, 2003) to September 30, 2005
Cash flow from operating activities:			
Net income (loss)	$ (1,028,674)	$ (650,053)	$ (4,788,982)
Adjustments to reconcile net income to net cash used in operating activities:			
Loss on sale of marketable securities	183	—	183
Gain on sale of unproved oil and gas property	(1,442,674)	—	(1,442,674)
Gain from extinguishment of debt	(383,531)	—	(383,531)
Debt issue costs and discount amortization	361,835	—	361,835
Depreciation	6,987	1,100	12,014
Expenses paid with stock issuance	264,500	—	722,000
Expenses paid with stock issuance obligation	—	—	304,500
Interest paid with stock issuance	44,711	—	44,711
Changes in operating assets and liabilities:			
Receivables	(2,155)	—	(2,155)
Prepaid expense	(15,000)	—	(15,000)
Deferred debt issue costs	(610,022)	—	(610,022)
Accounts payable	(92,937)	449,005	399,416
Net cash provided by (used in) operating activities	(2,896,777)	(199,948)	(5,928,951)
Cash flow from investing activities:			
Purchase of marketable securities	(365,087)	—	(365,087)
Deposits on unproved oil and gas property	(475,500)	—	(475,500)
Proceeds on sale of oil and gas property	1,930,083	—	1,930,083
Unproved oil and gas property additions	(1,412,673)	(5,257,617)	(3,570,778)
Restricted Cash	(100,000)	(135,000)	(235,000)
Purchase of equipment	(42,745)	—	(64,355)
Net cash provided by (used in) investing activities	(465,922)	(5,392,617)	(2,780,637)
Cash flow from financing activities:			
Proceeds from issuance of convertible debenture	6,024,633	1,000,000	7,024,633

Proceeds from issuance of common stock		922,376	3,698,092	3,597,468
Retirement of former management's stock		—	—	(27,000)
Proceeds from notes payable		80,000	625,000	2,321,000
Payments on notes payable		(1,252,848)	—	(1,937,469)
Net cash provided by financing activities:		5,774,161	5,323,092	10,978,632
Net increase in cash and equivalents		2,411,462	(269,473)	2,269,044
Cash and equivalents at beginning of period		149,027	291,445	291,445
Cash and equivalents at end of period		$ 2,560,489	$ 21,972	$ 2,560,489
Supplemental Disclosure of Cash Flow and Non-cash Investing and Financing Activity:				
Income tax paid		$ —	$ —	$ —
Interest paid		$ 81,750	$ —	$ 107,431
Non cash:				
Conversion of $350,000 convertible note into common stock		$ 394,711	$ —	$ 394,711
Acquisition of oil & gas interest in exchange for common stock		$ 600,000	$ —	$ 7,005,000
Contribution of oil & gas interest in exchange for stock issuance obligation		$ —	—	$ 194,000
Fees paid with stock		$ 309,211		$ 766,711

See accompanying notes to financial statements

Fellows Energy Ltd.
(A Development Stage Company)

Notes to Unaudited Financial Statements
September 30, 2005

Note 1 -Basis of Presentation and Nature of Operations

We have prepared the accompanying unaudited condensed financial statements in accordance with accounting principles generally accepted in the United States for interim financial information. They do not include all information and notes required by generally accepted accounting principles for complete financial statements. You should read these financial statements with our Annual Report on Form 10-KSB for the year ended December 31, 2004, as well as the 10-QSB for the quarters ended March, 31, 2005 and June 30, 2005. In our opinion, we have included all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation. Operating results for the quarters presented are not necessarily indicative of the results that you may expect for the full year.

We are engaged in the exploration, extraction, processing and reclamation of coal bed methane, natural gas, and oil projects in the western United States. We were incorporated in the state of Nevada on April 9, 2001 as Fuel Centers, Inc. On November 12, 2003, we changed our name to Fellows Energy Ltd. Our principal offices are located in Broomfield, Colorado.

Accumulated Other Comprehensive Income (Loss)

Accumulated other comprehensive income reflects changes in equity that result from transactions and economic events from non-operating sources. For the Company, such items consisted of unrealized holding gains and losses on market securities for the current period.

Earnings (Loss) per share

We compute basic and diluted earnings (loss) per share as net income or loss divided by the weighted average number of shares of common stock outstanding for the period. Diluted earnings per share is similar to basic earnings per share but also presents the dilutive effect on a per share basis of securities convertible into common shares (e.g. stock options, warrants and other convertible securities) as if they had been converted at the beginning of the periods presented. In periods in which we incur losses we exclude potential shares from convertible securities from the computation of diluted loss per share as their effect is antidilutive in those periods.

Stock Options

We account for stock options to employees in accordance with Accounting Principles Board Opinion No. 25 (“APB 25”), Accounting for Stock Issued to Employees, and related interpretations. Pursuant to APB No. 25, we record no compensation expense to employees on the date of grant because in issuing the grants we set the exercise price of the underlying stock at or above the market value of the stock on the date of the grant. Stock options granted to consultants are accounted for under the fair value method, in accordance with Statement of Financial Accounting Standards No. 123 (Statement 123), Accounting for Stock-Based Compensation.

Statement 123 and Statement 148, Accounting for Stock-Based Compensation Transition and Disclosure, require disclosure of pro forma information regarding net income and earnings per share. The Statements require that the information be determined as if we had accounted for employee stock options under the fair value method of the statements. We estimate the fair value of the options we grant at the date of grant using a Black-Scholes option pricing

model with the following weighted-average assumptions for the quarter ended September 30, 2005: a risk-free interest rate of 3%; no expected dividend; a volatility factor of 30.4%; and a maturity date of ten years.

For purposes of pro forma disclosures, we amortize to expense the estimated fair value of the options over the options' vesting period. Our pro forma information for the third quarter of 2005 is as follows (in thousands, except per share amounts).

	Nine Months Ended September 30, 2005	Nine Months Ended September 30, 2004
Net Income (loss) as reported	$ (1,029,309)	$ (650,053)
Deduct: Total stock based employee compensation expense determined under fair value based method for all awards	(51,100)	—
Pro forma net income (loss)	$ (1,080,309)	$ (650,053)
Basic and diluted earnings per share—as reported	$ -nil-	$ -nil-
Pro forma basic and diluted gain per share	$ -nil-	$ -nil-

The Black-Scholes option-pricing model was developed for use in estimating the fair value of traded options that have no vesting restrictions, are fully transferable, and are not subject to trading restrictions or blackout periods. In addition, option valuation models require the input of highly subjective assumptions, including the expected stock price volatility. Because our employee stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, it is our opinion that the existing models do not necessarily provide a reliable single measure of the fair value of our employee stock options.

In December 2004, the Financial Accounting Standards Board issued Statement of Financial Accounting Standard No. 123(R) (Statement 123(R)), *Accounting for Stock-Based Compensation*. Statement 123(R) establishes standards for the accounting for transactions in which an entity exchanges its equity instruments for goods or services. This statement focuses primarily on accounting for transactions in which an entity obtains employee services in share-based payment transactions. Statement 123(R) requires that the fair value of such equity instruments be recognized as an expense in the historical financial statements as services are performed. Prior to Statement 123(R), only certain pro forma disclosures of fair value were required. The provisions of this statement are effective at the beginning of the next fiscal year. Accordingly, we will adopt Statement 123(R) commencing with the quarter ending March 31, 2006. We believe the adoption of Statement 123(R) may have a material effect on our results of operations.

Oil and Gas Property

We follow the successful-efforts method of accounting for our oil and gas property. Under this method of accounting, we capitalize all property acquisition cost and cost of exploratory and development wells when incurred, pending determination of whether the well has found proved reserves. If an exploratory well does not find proved reserves, we charge to expense the cost of drilling the well. We include exploratory dry hole cost in cash flow from investing activities within the cash flow statement. We capitalize the cost of development wells whether productive or nonproductive.

We expense as incurred geological and geophysical cost and the cost of carrying and retaining unproved property. We provide an impairment allowance on a property-by-property basis when we determine that the unproved property will not be developed. We will provide depletion, depreciation and amortization (DD&A) of capitalized cost of proved oil and gas property on a field-by-field basis using the units-of-production method based upon proved reserves. In computing DD&A we will take into consideration restoration, dismantlement and abandonment cost and the anticipated proceeds from equipment salvage. When applicable, we will apply the provisions of Statement of

Financial Accounting Standards (FAS) No. 143, “Accounting for Asset Retirement Obligations,” which provides guidance on accounting for dismantlement and abandonment cost.

We review our long-lived assets for impairment when events or changes in circumstances indicate that an impairment may have occurred. In the impairment test we compare the expected undiscounted future net revenue on a field-by-field basis with the related net capitalized cost at the end of each period. We will calculate expected future cash flow on all proved reserves using a 15% discount rate and escalated prices. Should the net capitalized cost exceed the undiscounted future net revenue of a property, we will write down the cost of the property to fair value, which we will determine using discounted future net revenue. We have recorded no impairment charges on our oil and gas property as of September 30, 2005.

Impairment of Unproved (Non-Producing) Properties

Unproved properties are assessed periodically to determine whether or not they have been impaired. We will provide an impairment allowance on unproved property at any time we determine that a property will not be developed. At September 30, 2005, we considered our unproved properties economically and operationally viable and no unproved properties were surrendered or abandoned during the three months ended September 30, 2005, in accordance with FAS 19 and 144. Our recent activities in our properties are further described in Note 10.

Reclassifications

We have made certain reclassifications to the 2004 financial statements to conform with the 2005 financial statement presentation.

Note 2 - Going Concern

As shown in the accompanying financial statements, we have incurred significant operating losses since inception. From the inception of our oil and gas exploration business, we have not produced or sold any hydrocarbons. As of September 30, 2005 we have strengthened our financial resources. However, our ability to maintain profitability and positive cash flow is dependent upon our ability to exploit our mineral holdings, generate revenue from our planned business operations and control our exploration cost. We continue to seek additional financing. Should we not obtain adequate financing we may not be able to continue operations at our current scope of activity.

Note 3—Sale of Oil and Gas Property

In February 2005 we agreed to sell the Circus project for $1.98 million to an unrelated third party. We have received the full $1.98 million of the proceeds from the sale. We acquired the leases in October, 2004, with a total cost through the sale of $487,000. Additionally, we incurred $53,000 of closing cost on the sale.

Note 4 -Deposits

In July and August 2005, we entered into three separate agreements to option the acquisition interests in one producing and two exploration oil and gas properties. In connection with those options, we made deposits totaling $475,500, to negotiate and close acquisition agreements. One project known as the Carbon County project is currently producing and selling 30 million cubic feet of natural gas per month. The company has placed 300,000 on deposit to hold the property, 30,000 of which became non-refundable as of September 30, 2005. We expect to close on the project on or before November 30, 2005. We made deposits of $66,000, $65,000 and $44,500 on other projects for which we are negotiating. All the funds are fully refundable.

Note 5—Marketable Securities

The Company determines the appropriate classification of its investments in debt and equity securities at the time of purchase and reevaluates such determinations at each balance-sheet date. Debt securities are classified as held-to-maturity when the Company has the positive intent and ability to hold the securities to maturity. Debt securities for which the Company does not have the intent or ability to hold to maturity are classified as available-for-sale. Held-to-maturity securities are recorded as either short-term or long-term on the Balance Sheet based on contractual maturity date and are stated at amortized cost. Marketable securities that are bought and held principally for the purpose of selling them in the near term are classified as trading securities and are reported at fair value, with unrealized gains and losses recognized in earnings. Debt and marketable equity securities not classified as held-to-maturity or as trading, as classified as available-for-sale, and are carried at fair market value, with the unrealized gains and losses included in the determination of comprehensive income and reported in stockholders' equity.

The fair value of substantially all securities is determined by quoted market prices. The estimated fair value of securities for which there are no quoted market prices is based on similar types of securities that are traded in the market.

Note 6—Note Payable

In February 2005 we paid $750,000 principal of the 18% $1,500,000 note payable to JMG Exploration, Inc., plus accrued interest of $82,000. The remaining $750,000 was due on April 30, 2005.

In May 2005, we assigned our remaining 50% interest in the Gordon Creek and Weston County properties to JMG as full payment of the unpaid principal and accrued interest on the note. As part of the settlement agreement, JMG's commitment to spend $2,000,000 in exploration and drilling activity on the two projects by November 7, 2005 was terminated and JMG granted us the option to re-acquire our 50% ownership by June 30, 2005 for the amount of $391,000. We exercised this option in June 2005. Under this transaction, the Company removed itself from the liability of the note payable, and re-acquired the 50% ownership in the Gordon Creek and Weston County properties for $391,000. In connection with this transaction, we recorded a gain from extinguishment of debt of $383,531.

Note 7—Related Party Transactions

At March 31, 2005 we owed $35,000 on an unsecured, 8% demand note payable to an entity controlled by our CEO. During the quarter ending June 30, 2005, we borrowed $379,000 and paid down principal of $414,000 on the note, resulting in the paying off of the remaining balance owed plus interest of $500.

Note 8—Common Stock

In April 2005 we issued 2,999,265 shares of common stock for the following stock issuance obligations:

· 200,000 shares of common stock to Quaneco, LLC pursuant to a March 16, 2004 agreement;
· 50,000 shares of common stock to a business consultant pursuant to an August 1, 2004 agreement;
· 150,000 shares of common stock to a business consultant pursuant to a November 8, 2004 agreement;
· 100,000 shares of common stock to a business advisor pursuant to a January 10, 2005 agreement;
· 50,000 shares of common stock to a business consultant pursuant to a February 1, 2005 agreement;
· 2,449,265 shares of common stock on conversion of the 8% $350,000 convertible note issued September 9, 2003.

In April 2005, we issued 1,000,000 shares of common stock to Quaneco, LLC pursuant to a March 1, 2005 agreement as part of the consideration for the acquisition of the Kirby and Castle Rock projects. In accordance with the final purchase agreement, we have valued these shares at $0.60 per share. See Note 8.

On May 18, 2005, we closed on the private placement of $1,064,000 of securities. We incurred an estimated $141,000 of fees and cost, netting approximately $922,000. We sold 1,936,391 shares of common stock and 818,192 warrants. Each warrant entitles the holder to purchase one share of common stock for $1.00 until May 18, 2008. We also issued 81,819 of the same warrants to the placement agent as additional compensation. We have agreed to register the resale of the shares sold and the shares underlying the warrants with the U.S. Securities and Exchange Commission.

In June 2005, we issued a total of 200,000 shares of common stock in connection with agreements with a financial consultant.

During the third quarter ending September 30, 2005, we issued no new or additional shares of common stock.

Note 9—Convertible Debentures

On June 17, 2005, we closed a financing pursuant to a securities purchase agreement with three accredited investors for the issuance of $5,501,200 in face amount of debentures maturing at the end of the 27th month from the date of issuance, and three year warrants to purchase common stock of the company. The debentures bear no interest and the investors paid $3,849,685, after discounts of $1,651,515, for the debentures. A commission of 9% on the $3.85 million was paid in connection with the transaction, and we paid $100,000 in legal fees, resulting in net proceeds to the company of $3,403,267. The debentures are unsecured and we are obligated to pay 1/24th of the face amount of the debenture on the first of every month, starting October 1, 2005, which payment can be made in cash or in common stock. We may pay this amortization payment in cash or in stock at the lower of $0.60 per share (the Set Price) or 80% of the volume weighted average price of the stock for the five trading days prior to the repayment date. In the event that we make the payment in cash, we shall pay 110% of the monthly redemption amount. At any time after 90 days from the date that a registration statement registering the shares of common stock underlying the debentures and warrants is declared effective (the Effective Date), and if certain conditions are met, we have the right to redeem some or all of the debentures in a cash amount equal to 110% of the face amount of the debentures being redeemed. At any time, the debentures are convertible into common stock at the Set Price.

We issued warrants to the investors, expiring June 17, 2008, to purchase 4,584,334 shares of restricted common stock, exercisable at a per share of $0.649. In addition, the exercise price of the warrants will be adjusted in the event we issue common stock at a price below the exercise price, with the exception of any securities issued pursuant to a stock or option plan adopted by our board of directors, issued in connection with the debentures issued pursuant to the securities purchase agreement, or securities issued in connection with acquisitions or strategic transactions. Upon an issuance of shares of common stock below the exercise price, the exercise price of the warrants will be reduced to equal the share price at which the additional securities were issued and the number of warrant shares issuable will be

increased such that the aggregate exercise price payable for the warrants, after taking into account the decrease in the exercise price, shall be equal to the aggregate exercise price prior to such adjustment.

Warrants to purchase 250,000 shares, at the same price and for the same term as the warrants issued to the investors, have been issued to HPC Capital Management as additional compensation for its services in connection with the transaction with the investors.

In addition to the $1,651,515 cash discount, we also recorded a discount of $626,042 based on a Black-Scholes model valuation of the 4,584,334 warrants issued to the debenture holders and the 250,000 warrants issued to HPC Capital Management.

On September 21, 2005, we closed a financing pursuant to a securities purchase agreement with two accredited investors for the issuance of $3,108,000 in face amount of debentures maturing December 21, 2008, and three year warrants to purchase common stock of the company. The debentures do not accrue interest and the investors paid $2,174,947.52 for the debentures. A commission of 8% on $2,000,000 raised was paid to in connection with the transaction, and we placed $50,000 in escrow for the payment of future legal fees, resulting in net proceeds to the company of $1,964,947.52 before $39,000 in associated current legal fees. Net proceeds will be used for general working capital. The debentures are unsecured and we are obligated to pay 1/24th of the face amount of the debenture on the first of every month, starting January 1, 2006, which payment can be made in cash or in restricted common stock. We may pay this amortization payment in cash or in stock at the lower of $0.75 per share (the Set Price) or 80% of the volume weighted average price of the stock for the five trading days prior to the repayment date, provided that there is an effective registration statement and the monthly conversion price is greater of than $0.60. In the event that we make the payment in cash, we shall pay 110% of the monthly redemption amount. At any time after 90 days from the date that a registration statement registering the shares of common stock underlying the debentures and warrants is declared effective (the Effective Date), and if certain conditions are met, we have the right to redeem some or all of the debentures in a cash amount equal to 110% of the face amount of the debentures being redeemed. At any time, the debentures are convertible to restricted common stock at the Set Price.

We issued warrants to the investors, expiring September 21, 2008, to purchase 2,072,000 shares of restricted common stock, at a price per share of $0.80. The number of shares underlying the warrants equals 50% of the shares issuable on full conversion of the debentures at the set price (as if the debentures were so converted on September 21, 2005). In addition, the exercise price of the warrants will be adjusted in the event we issue common stock at a price below the exercise price, with the exception of any securities issued pursuant to a stock or option plan adopted by our board of directors, issued in connection with the debentures issued pursuant to the securities purchase agreement, or securities issued in connection with acquisitions or strategic transactions. Upon an issuance of shares of common stock below the exercise price, the exercise price of the warrants will be reduced to equal the share price at which the additional securities were issued and the number of warrant shares issuable will be increased such that the aggregate exercise price payable for the warrants, after taking into account the decrease in the exercise price, shall be equal to the aggregate exercise price prior to such adjustment.

Warrants to purchase 100,000 shares, at the same price and for the same term as the warrants issued to the investors, have been issued to HPC Capital Management as additional compensation for its services in connection with the transaction with the investors.

In addition to the $933,052 cash discount, we also recorded a discount of $614,905 based on a Black-Scholes model valuation of the 2,072,000 warrants issued to the debenture holders and the 100,000 warrants issued to HPC Capital Management.

Note 10—Unproved Oil and Gas Property

On April 14, 2005, we entered into a letter of intent to purchase the John’s Valley project, and we are under continuing negotiations to purchase the project or an interest in the project through an earn-in arrangement. We have made a payment of $300,000 toward the purchase. We are currently in negotiations to enter into an industry standard earn-in

agreement on the project.

On May 2, 2005, we entered into two option agreements with Thomasson Partner Associates, Inc. to participate in the Platte and Badger projects located in Garden and Keith Counties, Nebraska, and Stanley and Hughes Counties, South Dakota. Under the agreements, the initial project fee is $100,000 for the Platte project and $150,000 for the Badger project. Upon execution of definitive agreements we have paid Thomasson $80,000 for Platte, and $105,000 for Badger. This is made up of half of the initial project fees plus reimbursement of Land Sat cost of $30,000 each. In addition, there will be additional cost for a GeoChem survey on Platte and an air photo study on Badger for the amounts of $13,000 and $12,000 respectively. The geochemical survey and analysis has commenced on the Platte project in preparation for target delineation. We have made payments toward the total cost of these projects due to Thomasson by paying $50,000 for Platte and $75,000 for Badger. The total cost of these projects is $143,000 and $217,000 respectively.

In March 2005 we agreed, subject to customary closing conditions, with Quaneco to acquire a 12.5% working interest in the Kirby and Castle Rock Coal Bed Methane projects for $3,850,000 in cash and one million dollars worth of shares of restricted common stock. In April 2005 we issued Quaneco, 1,000,000 shares of our common stock in connection with this agreement. On June 23, 2005, we entered into a definitive purchase agreement with Quaneco and paid $500,000 toward the purchase, which vests in us a pro rata portion of the 12.5% interest, and we had until September 1, 2005 to pay additional amounts of the purchase price and vest in additional amounts. During the quarter ending September 30, 2005, we negotiated with Quaneco for an extension of the time to make payments, but have not yet finalized any extension. Under the terms of the agreement, we will participate in a 48 well drilling program during 2005 on the Kirby project that will extend out from an existing 16 well pilot program of previously drilled wells. The other working interest owners in the Kirby project include Quaneco (25.0%), Pinnacle Gas Resources (50%) and Galaxy Energy Corporation (12.5%). Operations continue on the dewatering and discharge of water from the first 16 wells drilled on the Kirby project. The construction of the pipeline to service the project is nearing completion. The water treatment plant is completed and under operation. We believe that production is imminent from the first 16 wells, while the drilling of the next 48 wells on Kirby is underway, and permits have been applied for for the drilling on the first 48 wells on Castle Rock.

On September 12, 2005, we entered into an agreement to purchase a gas field in Carbon County, Utah (the "Carbon County Project") currently producing approximately 30 million cubic feet of natural gas per month. The field comprises 5,953 gross acres (4,879 net acres) with three gas wells currently producing and has an additional six wells drilled that are presently shut-in. Production is derived from the Ferron Sandstone formation, and the gas is marketed into the adjacent gas pipeline operated by Questar Gas Resources. The field has potential for 20 additional well sites on 160 acre spacing on the undeveloped acreage. The property is adjacent to our Gordon Creek project and to the successful Drunkards Wash field originally developed by River Gas Corp. The closing of the purchase agreement is subject to numerous terms and conditions, including technical and legal due diligence which we are in the process of completing, and anticipate closing the acquisition by the end of November. A favorable engineering study has been completed by Sproule & Associates verifying the proven, developed producing reserves and undeveloped reserves.

On October 25, 2005, the Company announced that it had entered into a participation agreement with Mountain Oil and Gas, Inc., Creston Resources Ltd, and Homeland Gas and Oil Ltd. (collectively "Creston"), and is completing arrangements with private investors, whereby the Company will supply operating expertise and program supervision to earn working interests in up to 45 producing oil wells in the Uintah Basin of Utah. The Company will immediately commence a rework program to re-complete previously-completed zones and extend behind pipe reserves in the wells, located primarily in the prolific Altamont-Bluebell Field, which has produced over 350 million barrels of oil equivalent. Creston will retain the current or historical production while Fellows and the private investors will earn a variable percentage of the production increase resulting from the reworking operations. Work is scheduled to begin on the first four wells immediately, maintaining continuous operations until all wells have been brought to full potential.

Under the participation agreement, Fellows will begin reworking wells as necessary to revitalize production across the 9,000 acres that pertain to the wells. Due to the over-pressured, fractured nature of reservoir in the field, as well as the large vertical extent of potential pay zones, many of the wells have formation damage resulting from high drilling mud weights and cementing operations. These conditions have left many zones unable to produce to their potential. Fellows will employ a variety of conventional and innovative proprietary techniques to reduce the effects of formation damage and increase oil and gas recovery.

In mid-2004 we drilled the 10-33C2 well on the Johns Valley Project in Utah to its planned depth of 1,365 feet. We drilled through a potentially productive coal seam. We cored the well and have sent the core to a lab for evaluation. We have expensed the cost of this well as exploration expense. On April 14, 2005, we entered into a letter of intent to purchase the project, and we are under continuing negotiations to purchase the project or an interest in the project through an earn-in arrangement.

On August 12, 2005 we entered into a Purchase and Option Agreement with Western States Molybdenum Company ("Western States") for the purchase of all of its interests in oil and gas properties in Southern Utah. In the event we make the purchase, the negotiated price in $100,000, net of deposits previously made. We have through December 31, 2005 to exercise the option.

The last four agreements described above are the result of negotiations that took place during the quarter and were the subject of the $300,000, $66,000, $65,000 and $44,500 refundable deposits, respectively, described in Note 4 - Deposits.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Forward-Looking Statements

This report includes certain forward-looking statements. Forward-looking statements are statements that predict the occurrence of future events and are not based on historical fact. Forward-looking statements may be identified by the use of forward-looking terminology, such as "may", "shall", "will", "could", "expect", "estimate", "anticipate", "predict", "possible", "should", "continue", or similar terms, variations of those terms or the negative of those terms. We have written the forward-looking statements specified in the following information on the basis of assumptions we consider to be reasonable. However, we cannot predict our future operating results. Any representation, guarantee, or warranty should not be inferred from those forward-looking statements.

The assumptions we used for purposes of the forward-looking statements specified in the following information represent estimates of future events and are subject to uncertainty in economic, legislative, industry, and other circumstances. As a result, judgment must be exercised in the identification and interpretation of data and other information and in their use in developing and selecting assumptions from and among reasonable alternatives. To the extent that the assumed events do not occur, the outcome may vary substantially from anticipated or projected results. Accordingly we express no opinion on the achievability of those forward-looking statements. We cannot guarantee that any of the assumptions relating to the forward-looking statements specified in the following information are accurate. We assume no obligation to update any such forward-looking statements.

Overview

On January 5, 2004, we began operations as an oil and gas exploration company. We acquired interests in certain assets owned by Diamond Oil & Gas Corporation, in exchange for 3,500,000 shares of common stock. The transaction was deemed to have a value of $6,405,000. The assets included certain oil and gas projects, as well as the right to enter into the Exploration Services Funding Agreement with Thomasson Partner Associates, Inc. of Denver, Colorado. Diamond is controlled by our CEO, George S. Young. The operations we plan for 2005 include exploring leases we have acquired as well as seeking to acquire and explore additional property. Our goal is to discover substantial commercial quantities of oil and gas, including coalbed methane, on the properties.

In February 2005 we amended our Exploration Services Agreement with Thomasson Partner Associates. Thomasson Partner Associates provides large-scale exploration opportunities to the oil and gas industry. By this agreement Thomasson Partner Associates provides to us the first right to review and purchase up to a 50% interest (as amended, a 100% interest beginning in February 2005) in oil and natural gas exploration projects developed by Thomasson Partner Associates. Under the agreement, in 2005, Thomasson Partner Associates will present to us a minimum of eight project opportunities with the reasonable potential of at least 200 Bcf of natural gas reserves or 20 million barrels of oil reserves. We have the first right to review exploration projects developed by Thomasson Partner Associates and, after viewing a formal presentation regarding a project, we have a period of thirty days in which to acquire up to 100% of the project. We are not obligated to acquire any project. In consideration, in 2004 we paid to Thomasson Partner Associates a $400,000 overhead fee, and will pay an $800,000 fee in 2005. We also pay a fee for each project we acquire from Thomasson Partner Associates. The agreement continues year to year until either party gives 90 days written notice of termination. Projects acquired from Thomasson Partner Associates include the Weston County project in Wyoming, the Gordon Creek project in Utah, the Carter Creek project in Wyoming, the Circus project in Montana and the Bacaroo project in Colorado. In 2004 we incurred charges from Thomasson Partner Associates totaling $1,255,000, including the $400,000 overhead fee.

Operations Plans

During the next twelve months, we expect to pursue oil and gas operations on some or all of our property, including the acquisition of additional acreage through leasing, farmout or option and participation in the drilling of oil and gas wells. We intend to continue to evaluate additional opportunities in areas where we feel there is potential for oil and gas reserves and production and may participate in areas other than those already identified, although we cannot assure that additional opportunities will be available, or if we participate in additional opportunities, that those opportunities will be successful.

Our current cash position is not sufficient to fund our cash requirements during the next twelve months, including operations and capital expenditures. We intend to continue equity and/or debt financing efforts to support our current and proposed oil and gas operations and capital expenditures. We may sell interests in our properties. We cannot assure that continued funding will be available.

We have not entered into commodity swap arrangements or hedging transactions. Although we have no current plans to do so, we may enter into commodity swap and/or hedging transactions in the future in conjunction with oil and gas production. We have no off-balance sheet arrangements.

Our future financial results continue to depend primarily on (1) our ability to discover or purchase commercial quantities of oil and gas; (2) the market price for oil and gas; (3) our ability to continue to source and screen potential projects; and (4) our ability to fully implement our exploration and development program with respect to these and other matters. We cannot assure that we will be successful in any of these activities or that the prices of oil and gas prevailing at the time of production will be at a level allowing for profitable production.

Recent Activity

In February 2005 we agreed to sell the Circus project for $1.98 million to an unrelated third party. We completed the sale in June 2005. We acquired the leases in October 2004, with a total cost through the sale of $487,000. Additionally, we incurred $53,000 of closing cost on the sale.

In February 2005 we extended our agreement with a financial consultant and are obligated to issue an additional 50,000 shares to the consultant for compensation for his services, as well as a monthly fee of $7,500 for three months through April 2005. In April 2005, we further extended our agreement with the financial consultant through October 2005 on the same terms as the prior extension.

In March 2005 we agreed, subject to customary closing conditions, with Quaneco L.L.C. to acquire up to a 12.5% working interest in the Kirby and Castle Rock Coal Bed Natural Gas projects for $3,850,000 in cash and one million dollars worth of shares of restricted common stock. Under the terms of the agreement, we will participate in a 48-well drilling program during 2005 on the Kirby project that will extend out from an existing 16-well pilot program of previously drilled wells. The other working interest owners in the Kirby project include Quaneco (25.0%), Pinnacle Gas Resources (50%) and Galaxy Energy Corporation (12.5%). We are currently seeking financing to fund our participation in this project.

On May 2, 2005, we entered into two option agreements with Thomasson Partner Associates to participate in the Platte and Badger projects located in Garden and Keith Counties, Nebraska, and Stanley and Hughes Counties, South Dakota, respectively. Under the agreements, the initial project fee is $100,000 for the Platte project and $150,000 for the Badger project. Upon execution of definitive agreements we paid Thomasson Partner Associates $80,000 for Platte, and $105,000 for Badger. This amount represents approximately of the initial project fees plus reimbursement of Land Sat cost of $30,000 each. In addition, there will be additional costs for a GeoChem survey on Platte and an air photo study on Badger for the amounts of $13,000 and $12,000, respectively. The total cost of these projects is $143,000 and $217,000 respectively.

On May 18, 2005, we closed on $1,063,650 in equity financing and issued approximately 545,461 units, at a price of $1.95 per unit, each unit consisting of 3.55 shares of our common stock, and one and one-half Series A warrants to purchase our common stock. The units were sold to a limited number of accredited investors through a private placement memorandum and were exempt from registration under the Securities Act, pursuant to Section 4(2) of the Securities Act. We also agreed to pay the following to a placement agent: (1) a placement fee equal to 10% of the gross proceeds received from sales to certain investors identified by the placement agent; (2) a warrant or warrants, identical to the warrants contained in the units, equal to 15% of the number of units issued to certain investors identified by the placement agent, and (3) a non-accountable expense allowance of 3% of the aggregate gross proceeds of the private placement.

Each whole warrant entitles the holder to purchase one share of our common stock for a price of $1.00 per share for three years from the date of purchase of the unit. The warrants also contain limited anti-dilution rights. The warrants are subject to adjustment in the event of (1) any subdivision or combination of our outstanding common stock or (2)

any distribution by us to holders of common stock of (x) a stock dividend, or (y) assets (other than cash dividends payable out of retained earnings) to holders of common stock. In addition, until two years from the date the registration statement filed pursuant to the Registration Rights Agreement is declared effective, and except for certain issuances of our common stock including (A) pursuant to rights, warrants, convertible securities or options outstanding on the date of issuance of the warrants, (B) pursuant to the private placement, or (C) in other limited circumstances, if and when we issue or sell any common stock (including rights, warrants, convertible securities or options for its capital stock) for a consideration per share less than the per share purchase price of such common stock in the private placement, then we shall issue additional common stock to the investors so that the average per share purchase price of the shares of common stock issued to the investors (of only the common stock still owned by such investors) is equal to such other lower price per share.

In June 2005, we paid off the balance on our $1,500,000 loan to JMG Exploration, Inc., an affiliate of JED Oil, Inc., through the assignment of the our 50% interest in the Weston County and Gordon Creek projects.

On the Kirby and Castle Rock projects, operations continue on the dewatering and discharge of water from the first 16 wells drilled on the Kirby project. The construction of the pipeline to service the project is nearing completion. The water treatment plant is completed and under operation. We believe that production is imminent from the first 16 wells, while the drilling of the next 48 wells on Kirby is underway, and permits have been applied for for the drilling on the first 48 wells on Castle Rock.

On September 12, 2005, we entered into an agreement to purchase a gas field in Carbon County, Utah currently producing approximately 30 million cubic feet of natural gas per month. The field comprises 5,953 gross acres (4,879 net acres) with three gas wells currently producing and has an additional six wells drilled that are presently shut-in. Production is derived from the Ferron Sandstone formation, and the gas is marketed into the adjacent gas pipeline operated by Questar Gas Resources. The field has potential for 20 additional well sites on 160 acre spacing on the undeveloped acreage. The property is adjacent to our Gordon Creek project and to the successful Drunkards Wash field originally developed by River Gas Corp. The closing of the purchase agreement is subject to numerous terms and conditions, including technical and legal due diligence which we are in the process of completing, and anticipate closing the acquisition by the end of November. A favorable engineering study has been completed by Sproule & Associates verifying the proven, developed producing reserves and undeveloped reserves.

We will use the experience of our personnel who participated in the development of Drunkards Wash to increase current production and expand production in both the Ferron Sandstone and in the underlying coal bed methane seams that are not currently being exploited by the existing wells. We will immediately undertake to increase production in the existing wells, complete those wells in the coal for their coal bed methane potential, and thereafter drill additional wells on the acreage being acquired.

Oil & Gas Projects

Weston County, Wyoming

In November 2004 we executed a joint venture agreement with JMG Exploration, to drill our Weston County and Gordon Creek projects. Under the agreement, JMG Exploration will receive a 50% interest in exchange for spending $2,000,000 in exploration and drilling activity on the two projects by November 7, 2005. In addition, JMG Exploration loaned $1,500,000 to us with a short-term note. In connection with repayment of the JMG Exploration loan, we have assigned the remaining 50% interest in the Weston County project to JMG Exploration, subject to our right to reacquire those interests for approximately $391,000 by June 30, 2005, which right has been exercised. As part of the full settlement of the $1,500,000 note, JMG Exploration's commitment to spend $2,000,000 in exploration and drilling activity by November 7, 2005 has been terminated. In connection with this transaction, we recorded a gain from extinguishment of debt of $383,531.

The Weston County project is a 19,290-acre project on the east flank of the Powder River Basin. The prospect is a potential extension of an existing producing field. We are continuing our work and evaluation with JMG Exploration on permitting and other pre-drilling activities. In addition, we are targeting nearby locations with potential in the Minnelusa sandstone and Dakota channel sandstone formations.

Gordon Creek, Utah

JMG Exploration will also drill on the 5,242-acre Gordon Creek project, which we acquired from The Houston Exploration Company for $288,000. The Gordon Creek project is in an area of known coal resources in Carbon County in eastern Utah near other operating coal bed methane projects, such as the Drunkard's Wash Project, which our project personnel successfully drilled previously for River Gas Corporation.

Based on exploration results, JMG Exploration has indicated its intent to sell a portion of its working interest to Enterra Energy Trust in an arrangement under which JED Oil, Inc. under a development agreement with Enterra, will complete any development programs on the projects. In connection with repayment of the JMG Exploration loan, we have assigned the remaining 50% interest in the Gordon Creek project to JMG Exploration, subject to our right to reacquire those interests for approximately $390,000 by June 30, 2005, which right has been exercised.

Carter Creek, Wyoming

In 2004 we purchased the 10,678-acre Carter Creek Project in the southern Powder River Basin. We plan to commence drilling in the near future at the project, in which we have a 100% working interest. Based on our analysis of the geologic structure of this region, we anticipate productive sections in the Cretaceous, Niobrara, Turner (Frontier) and Mowry layers, in that several existing wells in the Carter Creek area currently produce oil.

Work continues to identify additional areas for leasing and drillsite delineation. We will continue our evaluation and preparation for drilling the fractured shales. It is likely that horizontal drilling methods will be identified as an effective technique to tap into the potential of this field.

Overthrust, Utah and Wyoming

In 2004 we optioned the Overthrust project for a 65% working interest in 183,000 acres of oil, gas and coal bed methane leases in northeastern Utah and southwestern Wyoming from Quaneco, an Oklahoma company. We plan to test the three identified coal seams that run through much of the area. Previous drilling has included seven exploratory wells that identified multiple coal seams of Tertiary and Cretaceous age that appear to be prospective for coal bed methane. Some of the coal is of similar age and depositional condition to other productive coal bed methane fields.

We drilled our first well in the project in 2004, the Crane 6-7, in Rich County, Utah. The well reached a total depth of 4280 feet. We cored coal and carbonaceous shale over a combined interval of 556 feet. In September 2004 we received the results from the gas desorption tests from the Spring Valley coal of the Frontier formation and the coal in the Bear River formation in the well. Results showed 253 cubic feet of gas per ton on an ash-free basis in the coal in the well. Lesser amounts of gas were present in the carbonaceous shale in the well. These tests corroborate earlier data that was generated by Quaneco, our partner on the project, suggesting that coal in an area of the project that lies a considerable distance north of the Crane 6-7 may contain between 200 and 400 cubic feet of gas per ton. We have expensed the cost of this well as exploration expense, although we may choose to re-enter the well at a later date. The overall results indicate the potential for coal in a much wider area to contain economic levels of coal bed methane, and will help to further guide our ongoing logging, geologic and drilling operations. We believe the Overthrust project has attractive coal bed methane potential, although additional exploration activity will be necessary to prove up gas reserves.

During the quarter ending September 30, 2005, we paid $275,000 to Quaneco representing payment obligations on the project and have negotiated extensions for various payment and work commitments in the future. We have progressed in the geologic evaluation of many of the potentially productive coal seams, and have delineated a number of areas for further work. Previous drilling activities have also identified reservoir quality sand which we believe has significant potential for conventional gas production if present in a favorable structural position. We will now review seismic

data covering the area to evaluate the conventional gas potential simultaneously with our ongoing activities to pursue the coal bed methane potential of the project. After evaluating the seismic data and further evaluation of the logs from previous drilling, we will design and implement the next drilling phase to target both conventional and coal bed methane gas.

Bacaroo, Colorado

In 2004 we optioned the Bacaroo project in Colorado through our affiliation with Thomasson Partner Associates. We believe the project is an opportunity to establish conventional oil and gas production with comparatively inexpensive drilling in areas of established production, while other projects being reviewed offer longer term, larger potential exploration opportunities. We are acquiring acreage in the prospect.

Leasing and seismic evaluation activities continue. One entire target area is now under lease, and two additional areas are now undergoing leasing. We will perform additional geologic evaluation and permitting work in preparation for drilling in early 2006.

Kirby and Castle Rock Projects, Powder River Basin, Montana

In March 2005 we agreed, subject to customary closing conditions, with Quaneco to acquire a 12.5% working interest in the Kirby and Castle Rock Coal Bed Methane projects for $3,850,000 in cash and one million dollars worth of shares of restricted common stock. We have paid $500,000 toward the purchase, which vests in us a pro rata portion of the 12.5% interest, and we have until September 1, 2005 to pay additional amounts of the purchase price and vest in additional amounts. During the quarter ending September 30, 2005, we negotiated with Quaneco for an extension of the time to make payments, but have not yet finalized any extension. Under the terms of the agreement, we will participate in a 48 well drilling program during 2005 on the Kirby project that will extend out from an existing 16 well pilot program of previously drilled wells. We will have ownership in the previously drilled wells, which are currently being dewatered and are expected to commence production later in the near future. The other working interest owners in the Kirby project include Quaneco (25.0%), Pinnacle Gas Resources (50%) and Galaxy Energy Corporation (12.5%).

We plan to participate in a 48 well drilling program during 2005 on the Castle Rock project that will extend out from four previously drilled core holes. The other working interest owners in the Castle Rock Project include Quaneco (25.0%), Enterra Energy Trust (43.75%), Carrizo (6.25%) and Galaxy Energy Corporation (12.5%).

The Powder River Basin coalfield of northeastern Wyoming and southeastern Montana is an unconventional gas play that offers an unusual combination of comparatively moderate risk and large economic potential. The large coal deposits of the Powder River Basin are one of the greatest accumulations of coal in the world. These coal deposits contain a large resource of biogenic coal bed methane associated with numerous thick, laterally continuous, relatively shallow (less than 3,000 feet deep) Tertiary coal beds.

The Kirby project is an extension of the Powder River Basin coal bed methane play, which produces from the Tongue River Member of the Tertiary Fort Union Formation, on the western margin of the Basin north of Sheridan, Wyoming. This portion of the Basin has already seen considerable production from property owned and managed by Huber Oil & Gas at Prairie Dog Field which is on the Wyoming side, and Fidelity Oil & Gas at CX Field which straddles the Montana/Wyoming border. The Kirby project has 95,000 acres of fee, state and federal leasehold about 10 miles north of Decker, Montana. Fidelity’s CX Field is about 6 miles south of the southern boundary of the prospect.

A 16-well pilot well program has been drilled on the Kirby acreage and has continued well into its dewatering phase. This pilot program will test the productivity of the Wall and Flowers-Goodale coal formations. Gas content data from mud logs and cores taken over these zones indicates that the prospective coal is fully saturated with gas, which we believe will lead to a short period of dewatering before commercial gas production volume is achieved. The engineering firm Sproule Associates, Inc. has been retained to perform a resource evaluation of the Kirby project. We believe hundreds of wells could potentially be drilled on the 95,000-acre Kirby project.

The Castle Rock project is an extension of the Powder River Basin play on the eastern margin of the Basin north of Gillette, Wyoming. This portion of the Basin is where most of the Basin's production has occurred. The Castle Rock project has 140,000 acres of fee, state and federal leasehold along the Pumpkin Creek drainage about 20 miles west of Broadus, Montana. The eastern and northern boundaries of the prospect are the outcrops of the Sawyer and Flowers Goodale Coals. Sproule also conducted a resources evaluation of the Castle Rock project with favorable results.

Circus Project, Montana

In May 2004, we optioned the Circus project through our affiliation with Thomasson Partner Associates. In February 2005 we agreed to sell the Circus project for $1.98 million to an unrelated third party. We completed the sale in June 2005. We acquired the leases in October, 2004, with a total cost through the sale of $487,000. Additionally, we incurred $53,000 of closing cost on the sale.

Johns Valley Project, Utah

In early 2004 we acquired an agreement with Johns Valley Limited Partnership whereby we have the option to earn 70% working interest in 25,201 acres of oil and gas leases from the Utah School and Institutional Trust Lands Administration. The option, which expired in October 2004, was for fifteen oil and gas leases that were for terms of ten years. Due to permitting delays and other operating parameters in the field, we are negotiating to restructure the potential option and the timing and amounts of our work commitments as provided under the option assignment agreement.

In mid-2004 we drilled the 10-33C2 well in this project to its planned depth of 1,365 feet. We drilled through a potentially productive coal seam. We cored the well and have sent the core to a lab for evaluation. We have expensed the cost of this well as exploration expense.

On April 14, 2005, we entered into a letter of intent to purchase the project, and we are under continuing negotiations to purchase the project or an interest in the project through an earn-in arrangement.

Present Activity

We described our present activity in detail by project in Oil and Gas Projects, above. We have interests in wells currently drilling in the Kirby and Castle Rock projects. Currently, we have interests in 16 wells that are commencing the production phase and in drilling programs with 96 wells during 2005. We also have plans to finance and drill on the Overthrust project, the Carter Creek project, the Bacaroo project and the Johns Valley project during 2005. We expect our partner, JMG Exploration, will also be drilling on the Weston County and Gordon Creek projects in 2005. We are seeking capital which we need in order to finance these projects.

Results of Operations

Revenue. Throughout 2004 and 2005 to date, we earned no revenue from our exploration activity on our oil and gas property or from other operations.

Operating expense. For the quarter ended September 2005, our operating expense was $1,453,000, compared to $256,000 in the September 2004 quarter. The expense for both quarters came from oil and gas exploration, salaries, business advisory services, legal and professional fees, travel, occupancy and investor relations expense. The expense increased because of costs of capital and other business advisory services.

Gain on sale of property. In the March 2005 quarter we earned a $1,437,000 gain on the sale of the Circus project, which we sold for $1,977,000. Our cost on the leases was $487,000. Additionally, we incurred $53,000 of closing cost.

Interest expense. We incurred interest expense of $46,000 in the September 2005 quarter compared to $35,000 in the September 2004 quarter. Interest increased because of an increase in our debt between the two quarters.

Liquidity and Capital Resources

In 2004 we incurred a loss of $3,760,000. In the quarter ended September 30, 2005, we incurred a net loss of $1,029,000. At September 30, 2005, we had $2,560,000 of cash, total current assets of $2,942,000 and current liabilities of $341,000. In February 2005 we sold the Circus project for $1.98 million to an unrelated third party. We acquired the leases in October, 2004, with a total cost through the sale of $487,000. Additionally, we incurred $53,000 of closing cost on the sale. On May 18, 2005, we closed on the private placement of $1,064,000 of securities. We incurred an estimated $141,000 of fees and cost, netting approximately $922,000. We sold 1,936,391 shares of common stock and 818,192 warrants. Each warrant entitles the holder to purchase one share of common stock for $1.00 until May 18, 2008. We also issued 81,819 of the same warrants to the placement agent as additional compensation. On June 17, 2005, we closed a financing pursuant to a securities purchase agreement with three accredited investors for the issuance of $5.5 million in face amount of debentures maturing at the end of the 27th month from the date of issuance, and three year warrants to purchase common stock of the company. The debentures do not accrue interest and the investors paid $3.85 million for the debentures. A commission of 9% on the $3.85 million was paid in connection with the transaction, and we paid $30,000 of the investor's counsel's legal fees, resulting in net proceeds to the company of $3.4 million. Net proceeds will be used for general working capital.

As shown in the accompanying financial statements, we have incurred significant operating losses since inception. From the inception of our oil and gas exploration business, we have not produced or sold any hydrocarbons. Although we have acquired an option of interest in the Kirby and Castle Rock projects which are now going into production, we have no assets at present which are able to generate oil & gas sales without further expenditures for the development of the reserves. Our ability to maintain profitability and positive cash flow is dependent upon our ability to exploit our mineral holdings, generate revenue from our planned business operations and control our exploration cost. To fully carry out our business plans we need to raise a substantial amount of additional capital, which we are currently seeking. We can give no assurance that we will be able to raise such capital. We have limited financial resources until such time that we are able to generate positive cash flow from operations. Our ability to maintain profitability and positive cash flow is dependent upon our ability to locate profitable natural gas or oil properties, generate revenue from our planned business operations, and control exploration cost. Should we be unable to raise adequate capital or to meet the other above objectives, it is likely that we would have to substantially curtail our business activity, and that our investors would incur substantial losses of their investment.

June 2005 private placement

On June 17, 2005, we closed a financing pursuant to a securities purchase agreement with three accredited investors for the issuance of $5,501,199.95 in face amount of debentures maturing June 17, 2008, and three year warrants to purchase our common stock. The debentures do not accrue interest and the investors paid $3,849,685 for the debentures. A commission of 9% on the $3,849,685 was paid by us to HPC Capital Management, a registered broker-dealer, in connection with the transaction, and we paid $100,000 in expenses and fees including $30,000 of the investors’ counsel’s legal fees, resulting in net proceeds to us of $3,403,267.35. Net proceeds will be used by us for general working capital.

The debentures are unsecured and we are obligated to pay 1/24th of the face amount of the debenture on the first of every month, starting October 1, 2005, which payment can be made in cash or in shares of our common stock. We may pay this amortization payment in cash or in stock at the lower of $0.60 per share or 80% of the volume weighted average price of our stock for the five trading days prior to the repayment date. In the event that we make the payment in cash, we shall pay 110% of the monthly redemption amount. For the months of October and November 2005, we elected to make the monthly payments in cash.

Except as provided in the succeeding paragraph and to the extent any debentures remain outstanding, at any time, the debentures are convertible into shares of our common stock at $0.60 per share.

At any time after January 15, 2006, and if certain conditions are met, we have the right to redeem some or all of the debentures in a cash amount equal to 110% of the face amount of the debentures being redeemed.

If the closing price for our common stock exceeds $1.50 for 20 consecutive trading days, we can require the holders to convert some or all of the debentures at $0.60.

We issued warrants to the investors, expiring June 17, 2008, to purchase 4,584,334 shares of restricted common stock, exercisable at a per share of $0.649. In addition, the exercise price of the warrants will be adjusted in the event we issue common stock at a price below the exercise price, with the exception of any securities issued pursuant to a stock or option plan adopted by our board of directors, issued in connection with the debentures issued pursuant to the securities purchase agreement, or securities issued in connection with acquisitions or strategic transactions. Upon an issuance of shares of common stock below the exercise price, the exercise price of the warrants will be reduced to equal the share price at which the additional securities were issued and the number of warrant shares issuable will be increased such that the aggregate exercise price payable for the warrants, after taking into account the decrease in the exercise price, shall be equal to the aggregate exercise price prior to such adjustment.

Warrants to purchase 250,000 shares, at the same price and for the same term as the warrants issued to the investors, have been issued to HPC Capital Management as additional compensation for its services in connection with the transaction with the investors.

If in any period of 20 consecutive trading days our stock price exceeds 250% of the warrants' exercise price, all of the warrants shall expire on the 30th trading day after we send a call notice to the warrant holders. If at any time after one year from the date of issuance of the warrants there is not an effective registration statement registering, or no current prospectus available for, the resale of the shares underlying the warrants, then the holder may exercise the warrant at such time by means of a cashless exercise. In the event the investors exercise the warrants on a cashless basis, then we will not receive any proceeds.

The conversion price of the debentures and the exercise price of the warrants may be adjusted in certain circumstances such as if we pay a stock dividend, subdivide or combine outstanding shares of common stock into a greater or lesser number of shares, or take such other actions as would otherwise result in dilution of the investors' position.

The investors have agreed to restrict their ability to convert their debentures or exercise their warrants and receive shares of our common stock such that the number of shares of common stock held by them in the aggregate and their affiliates after such conversion or exercise does not exceed 4.99% of the then issued and outstanding shares of common stock.

September 2005 Private Placement

On September 21, 2005, we closed a financing pursuant to a securities purchase agreement with two accredited investors for the issuance of $3,108,000 in face amount of debentures maturing December 20, 2008, and three year warrants to purchase our common stock. The debentures do not accrue interest and the investors paid $2,174,947.52 for the debentures. A commission of 8% on $2,000,000 raised was paid by us to HPC Capital Management, a registered broker-dealer, in connection with the transaction and we placed $50,000 in escrow for the payment of future legal fees in connection with our registration statement, resulting in net proceeds to us of $1,964,947.52, before our legal fees. Net proceeds will be used by us for general working capital.

The debentures are unsecured and we are obligated to pay 1/24th of the face amount of the debenture on the first of every month, starting January 1, 2006, which payment can be made in cash or in shares of our common stock. We may pay this amortization payment in cash or in stock at the lower of $0.75 per share or 80% of the volume weighted average price of our stock for the five trading days prior to the repayment date. In the event that we make the payment in cash, we shall pay 110% of the monthly redemption amount.

Except as provided in the succeeding paragraph and to the extent any debentures remain outstanding, at any time, the debentures are convertible into shares of our common stock at $0.75 per share.

At any time after 90 days from the date that a registration statement registering the shares of common stock underlying the debentures and warrants is declared effective, and if certain conditions are met, we have the right to redeem some or all of the debentures in a cash amount equal to 110% of the face amount of the debentures being redeemed.

After the registration statement registering the shares of common stock underlying the debentures and warrants is declared effective, if the closing price for our common stock exceeds $1.875 for 20 consecutive trading days, we can require the holders to convert some or all of the debentures at $0.75.

In the event of default, the investors may require payment, which shall be the greater of: (A) 130% of the principal amount of the face amount of the debenture to be prepaid, or (B) the principal amount of the debenture to be prepaid, divided by the conversion price on (x) the date the default amount is demanded or otherwise due or (y) the date the

default amount is paid in full, whichever is less, multiplied by the closing price on (x) the date the default amount is demanded or otherwise due or (y) the date the default amount is paid in full, whichever is greater

We issued warrants to the investors, expiring September 21, 2008, to purchase 2,172,000 shares of restricted common stock, exercisable at a per share of $0.80. In addition, the exercise price of the warrants will be adjusted in the event we issue common stock at a price below the exercise price, with the exception of any securities issued pursuant to a stock or option plan adopted by our board of directors, issued in connection with the debentures issued pursuant to the securities purchase agreement, or securities issued in connection with acquisitions or strategic transactions. Upon an issuance of shares of common stock below the exercise price, the exercise price of the warrants will be reduced to equal the share price at which the additional securities were issued and the number of warrant shares issuable will be increased such that the aggregate exercise price payable for the warrants, after taking into account the decrease in the exercise price, shall be equal to the aggregate exercise price prior to such adjustment.

Warrants to purchase 100,000 shares, at the same price and for the same term as the warrants issued to the investors, have been issued to HPC Capital Management as additional compensation for its services in connection with the transaction with the investors.

After the effective date of this registration statement, if in any period of 20 consecutive trading days our stock price exceeds 250% of the warrants' exercise price, all of the warrants shall expire on the 30th trading day after we send a call notice to the warrant holders. If at any time after one year from the date of issuance of the warrants there is not an effective registration statement registering, or no current prospectus available for, the resale of the shares underlying the warrants, then the holder may exercise the warrant at such time by means of a cashless exercise. In the event the investors exercise the warrants on a cashless basis, then we will not receive any proceeds.

The conversion price of the debentures and the exercise price of the warrants may be adjusted in certain circumstances such as if we pay a stock dividend, subdivide or combine outstanding shares of common stock into a greater or lesser number of shares, or take such other actions as would otherwise result in dilution of the investors' position.

The investors have agreed to restrict their ability to convert their debentures or exercise their warrants and receive shares of our common stock such that the number of shares of common stock held by them in the aggregate and their affiliates after such conversion or exercise does not exceed 4.99% of the then issued and outstanding shares of common stock.

Cash flow. In the September 2005 quarter we used $2,897,000 in our operating activity. We used $466,000 in investing activity for property and option acquisitions, and obtained $5,774,000 in financing activity from capital obtained through financings. We increased our June 30, 2005 cash balance of $2,503,000 to $2,560,000 at September 30, 2005.

Critical Accounting Policies and Estimates

Our Management's Discussion and Analysis of Financial Condition and Results of Operations section discusses our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expense during the reporting period. On an on-going basis, we evaluate our estimates and judgments, including those related to revenue recognition, accrued expense, financing operations, contingencies and litigation. We base our estimates and judgments on historical experience and on various other factors that we believe to be reasonable under the circumstances. Our estimates and judgments form the basis for determining the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. These carrying values are some of the most significant accounting estimates inherent in the preparation of our financial statements. These accounting policies are described in relevant sections in this discussion and in the notes to the financial statements included in our December 31, 2004 Form 10-KSB Annual Report.

Item 3. Controls and Procedures

a) *Evaluation of Disclosure Controls and Procedures:* As of September 30, 2005, our management carried out an evaluation, under the supervision of our Chief Executive Officer and Chief Financial Officer of the effectiveness of the design and operation of our system of disclosure controls and procedures pursuant to the Securities and Exchange Act, Rule 13a-15(e) and 15d-15(e) under the Exchange Act). Based on that evaluation, our chief executive officer and chief financial officer concluded that our disclosure controls and procedures are effective to provide reasonable assurance that information we are required to disclose in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms, and that such information is accumulated and communicated to our management, including our chief executive officer and chief financial officer, as appropriate, to allow timely decisions regarding required disclosure.

b) *Changes in internal controls:* There were no changes in internal controls over financial reporting that occurred during the period covered by this report that have materially affected, or are reasonably likely to materially effect, our internal control over financial reporting.

Part II: Other Information

Item 1. Legal Proceedings

From time to time, we may become involved in various lawsuits and legal proceedings which arise in the ordinary course of business. However, litigation is subject to inherent uncertainties, and an adverse result in these or other matters may arise from time to time that may harm our business. Except as described in our annual report on Form 10-KSB, filed with the Commission on June 30, 2005, we are currently not aware of any such legal proceedings or claims that we believe will have, individually or in the aggregate, a material adverse affect on our business, financial condition or operating results.

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

On September 21, 2005, we closed a financing pursuant to a securities purchase agreement with two accredited investors for the issuance of $3,108,000 in face amount of debentures maturing December 20, 2008, and three year warrants to purchase our common stock. The debentures do not accrue interest and the investors paid $2,174,947.52 for the debentures. A commission of 8% on $2,000,000 raised was paid by us to HPC Capital Management, a registered broker-dealer, in connection with the transaction and we placed $50,000 in escrow for the payment of future legal fees in connection with our registration statement, resulting in net proceeds to us of $1,964,947.52, before our legal fees. Net proceeds will be used by us for general working capital.

The debentures are unsecured and we are obligated to pay 1/24th of the face amount of the debenture on the first of every month, starting January 1, 2006, which payment can be made in cash or in shares of our common stock. We may pay this amortization payment in cash or in stock at the lower of $0.75 per share or 80% of the volume weighted average price of our stock for the five trading days prior to the repayment date. In the event that we make the payment in cash, we shall pay 110% of the monthly redemption amount.

Except as provided in the succeeding paragraph and to the extent any debentures remain outstanding, at any time, the debentures are convertible into shares of our common stock at $0.75 per share.

At any time after 90 days from the date that a registration statement registering the shares of common stock underlying the debentures and warrants is declared effective, and if certain conditions are met, we have the right to redeem some or all of the debentures in a cash amount equal to 110% of the face amount of the debentures being redeemed.

After the registration statement registering the shares of common stock underlying the debentures and warrants is declared effective, if the closing price for our common stock exceeds $1.875 for 20 consecutive trading days, we can require the holders to convert some or all of the debentures at $0.75.

In the event of default, the investors may require payment, which shall be the greater of: (A) 130% of the principal amount of the face amount of the debenture to be prepaid, or (B) the principal amount of the debenture to be prepaid, divided by the conversion price on (x) the date the default amount is demanded or otherwise due or (y) the date the default amount is paid in full, whichever is less, multiplied by the closing price on (x) the date the default amount is demanded or otherwise due or (y) the date the default amount is paid in full, whichever is greater

We issued warrants to the investors, expiring September 21, 2008, to purchase 2,172,000 shares of restricted common stock, exercisable at a per share of $0.80. In addition, the exercise price of the warrants will be adjusted in the event we issue common stock at a price below the exercise price, with the exception of any securities issued pursuant to a stock or option plan adopted by our board of directors, issued in connection with the debentures issued pursuant to the securities purchase agreement, or securities issued in connection with acquisitions or strategic transactions. Upon an

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Item 3. Defaults Upon Senior Securities

None.

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

None.

Item 5. Other Information

None.

Item 6. Exhibits

31.1 Certification of Chief Executive Officer pursuant to Rule 13a-14 and Rule 15d-14(a), promulgated under the Securities and Exchange Act of 1934, as amended

31.2 Certification of Chief Financial Officer pursuant to Rule 13a-14 and Rule 15d 14(a), promulgated under the Securities and Exchange Act of 1934, as amended

32.1 Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Chief Executive Officer)

32.2 Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Chief Financial Officer)

Signatures

In accordance with the requirements of the Securities Exchange Act of 1934, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

FELLOWS ENERGY LTD.

Date: February 13, 2006

By: /s/ *GEORGE S. YOUNG*

George S. Young
Chief Executive Officer (Principal Executive Officer Principal Accounting Officer and Principal Financial Officer)