

TETON PETROLEUM CO  
Form 10-K/A  
May 09, 2005

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549  
FORM 10-K/A**

[X] ANNUAL REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE FISCAL YEAR ENDED DECEMBER 31, 2004.

Commission File No. 000-31170

**TETON PETROLEUM COMPANY**  
(Exact name of registrant as specified in its charter)

DELAWARE  
(State or other jurisdiction  
of incorporation or organization)

1482290  
(I.R.S. Employer  
Identification No.)

1600 Broadway, Suite 2400  
Denver, Co. 80202 - 4921  
(Address of principal executive offices)

Registrant's telephone number: 303.542.1878

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

Securities registered pursuant to Section 12(g) of the Exchange Act:

| <u>Title of Class</u> | <u>Name of Each Exchange on Which Registered</u> |
|-----------------------|--|
| Common Stock          | American Stock Exchange                          |

Indicate by a check mark whether the registrant (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days. YES [X] NO [ ]

Indicate by a check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, 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. [ X ]

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

The issuer's revenue for its most recent fiscal year was \$0

As of June 30, 2004, approximately 9,114,663 shares of common stock were outstanding. The aggregate market value of the common stock held by non-affiliates of the issuer, as of June 30, 2004, was approximately \$21,060,742 based on the closing bid of \$2.45 for the issuer's common stock as reported on the American Stock Exchange. Shares of

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common stock held by each director, each officer named in Item 12, and each person who owns 10% or more of the outstanding common stock have been excluded from this calculation in that such persons may be deemed to be affiliates. The determination of affiliate status is not necessarily conclusive.

As of Friday, May 4, 2005 the issuer had 10,022,996 shares of common stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE - NONE

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**EXPLANATORY NOTE**

This Form 10-K/A is being filed to amend and restate Item 9A of Part II of the Annual Report on Form 10-K for the fiscal year ended December 31, 2004, which was filed with the Securities and Exchange Commission on March 31, 2005, by Teton Petroleum Company. This amendment responds to certain comments of the Staff of the Securities and Exchange Commission in connection with its review of the Registrants' Annual Report on Form 10-K for the fiscal year ended December 31, 2004. This amendment supplements the disclosure controls and procedures and provides additional detail concerning controls and procedures that were not completely effective during the year ended December 31, 2004. All other information included in the original on Form 10-K, as filed on March 31, 2005, remains unchanged.

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**FORM 10-K/A**  
**FOR THE FISCAL YEAR ENDED DECEMBER 31, 2004**

**INDEX**

|   | Page |
|---|------|
| <b>PART I</b>   |      |
| Item 1. Business  | 3    |
| Item 2. Properties  | 9    |
| Item 3. Legal Proceedings   | 10   |
| Item 4. Submission of Matters to a Vote of Security Holders   | 10   |
| <b>PART II</b>  |      |
| Item 5. Market for the Registrant's Common Equity and Related Stockholder Matters                       | 11   |
| Item 6. Selected Financial Data   | 13   |
| Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations           | 13   |
| Item 7A. Quantitative and Qualitative Disclosures about Market Risks                                    | 18   |
| Item 8. Financial Statements and Supplementary Data   | 19   |
| Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure            | 54   |
| Item 9A. Controls and Procedures  | 54   |
| Item 9B. Other Information  | 54   |
| <b>PART III</b>   |      |
| Item 10. Directors and Executive Officers of the Registrant   | 55   |
| Item 11. Executive Compensation   | 58   |
| Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters | 60   |
| Item 13. Certain Relationships and Related Transactions   | 61   |
| Item 14. Principal Accountant Fees and Services   | 61   |
| <b>PART IV</b>  |      |
| Item 15. Exhibits and Financial Statement Schedules   | 63   |
| <b>SIGNATURES</b>   |      |

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## PART I

### Caution Concerning Forward-Looking Statements

We have included in this report, statements which are intended as “forward-looking statements” under the Private Securities Litigation Reform Act of 1995. These include statements that are not simply a statement of historical fact but describe what we “believe,” “anticipate,” or “expect” will occur. We caution you not to place undue reliance on the forward-looking statements made in this report. Although we believe these statements are reasonable, there are many factors, which may affect our expectation of our operations. These factors include, among other things, the following:

- general economic conditions
- the market price of, and demand for, oil and natural gas
- our ability to service future indebtedness
- our ability to raise additional equity capital, obtain debt financing, or generate sufficient revenues to fund our operating and development plan
  - our success in completing development and exploration activities
  - expansion and other development trends of the oil and gas industry
  - our present company structure
  - our accumulated deficit
- acquisitions and other business opportunities that may be presented to and pursued by us
  - our ability to integrate our acquisitions into our company structure
  - changes in laws and regulations

### Summary

Until July 16, 2004 Teton Petroleum Company (“Teton,” the “Company,” “We” or “Us”) through a consolidated Russian subsidiary ZAO Goloil (“Goloil”), was primarily engaged in oil and gas exploration, development, and production in Western Siberia, Russia.

For the first six months of 2004 Teton’s efforts were concentrated on negotiating and finalizing the sale of Goloil.

Effective July 1, 2004, for accounting purposes, Teton sold its interest in Goloil and recorded a gain of \$13,087,000.

Since the sale of Goloil the Company has focused on evaluating potential acquisitions of oil and gas properties located in the United States, Russia and the Commonwealth of Independent States.

During December 2004 the Company entered into a binding letter of intent and subsequent to year-end entered into a formal contract to acquire up to 180,000 acres of oil and gas leases in a significant block of acreage in North America, subject to the completion of due diligence and other conditions. See subsequent events on Page 19.

On February 15, 2005, in a second transaction, the Company purchased 25% of the membership interest of Piceance Gas Resources, LLC, a Limited Liability Company whose primary asset is oil and gas rights and leasehold assets covering approximately 6,300 acres in the Piceance Basin of Western Colorado. See subsequent events on Page 19.

## Item 1. BUSINESS.

### Background

The Company is an independent energy company engaged primarily in the development, production and marketing of natural gas and oil in North America. We intend to increase stockholder value by profitably growing reserves and production, primarily through drilling operations. We seek high quality exploration and development projects with potential for providing long-term drilling inventories that generate high returns.

The Company's current operations are focused in the Rocky Mountain Region of the United States. From its inception until 2004, the Company was primarily engaged in oil and gas exploration, development, and production in Western Siberia, Russia. In July 2004, the Company's shareholders voted to sell its Russian operations to the Company's Russian partner. The sale, which was deemed effective as of July 1, 2004, for accounting purposes, resulted in our reporting a gain of \$13,087,000. The purchase price for our 35.30% interest in Goloil was \$8,960,000 in cash, which was received during August 2004. Goloil also repaid advances made by the Company to Goloil totaling \$6,040,000. The advances were made to Goloil by the Company to finance our 50% share of Goloil's capital expenditures and currently bore interest at the rate of 8% per annum. The gross proceeds of the two transactions to the Company totaled \$15,000,000.

Between July 2004 and January 2005 the Company actively pursued opportunities in North America and abroad in order to redeploy the cash generated in the sale of its Goloil asset. In December 2004 and again in January 2005, the Company reported the signing of a binding letter of intent and definitive purchase agreement, respectively, for up to 180,000 acres located in North America. The Company made an additional purchase in February 2005 of a 25% interest in Piceance Gas Resources, LLC ("PGR") which owns approximately 6,300 acres in the Piceance Basin, located northwest of the Grand Valley Field in Western Colorado. The purchase price of the 25% interest is \$5.25 million cash and 450,000 unregistered shares of Teton common stock. Teton also issued PGR Partners, LLC warrants to purchase 200,000 shares of Teton common stock at an exercise price of \$2.00 per share, exercisable for five years. Please read Subsequent Events on Page 19.

### Available Information

The Company's Internet address is [www.tetonpetroleum.com](http://www.tetonpetroleum.com). Electronic copies of the Company's annual report on Form 10-K, quarterly reports on Form 10-Q, and current reports on Form 8-K, and amendments to those reports are available free of charge by visiting the "Financials" section of [www.tetonpetroleum.com](http://www.tetonpetroleum.com). These reports are posted as soon as reasonably practicable after they are electronically filed with the Securities and Exchange Commission. Additional information including the Company's Code of Business Conduct and Ethics is also available on our website.

### Business Strategy

The Company's objective is to expand its natural gas and oil reserves, production and revenues through a strategy that includes the following key elements:

*Initiate drilling operations.* With the acquisition of the Piceance acreage, the Company intends to initiate drilling operations beginning in the second quarter of 2005. PGR's business plan for 2005 includes drilling a minimum of eight wells. PGR is the operator of record in our Piceance Basin Project. Teton owns a 25% interest in PGR. Teton may operate in other areas. The Company understands that there is significant competition for the acquisition of producing properties and therefore growing the Company through drilling opportunities is also essential.





*Acquire producing properties.* The Company's acquisition efforts are focused on properties that fit well within existing operations or in areas where the Company is establishing new operations or where it believes that a base of existing production will produce an adequate foundation for economies of scale necessary to grow a business within a geography or business segment.

*Pursue geographic expansion.* The Company and its key executives have operated both within the United States and internationally. The Company believes that its international experience provides it with a significant competitive edge relative to similarly situated organizations that tend to remain localized in their operations and focus. The Company believes that geographic diversification provides the ultimate hedge to being able to operate an energy concern during the peaks and troughs of the energy business cycle.

*Reduce risks inherent in oil and natural gas development and marketing.* An integral part of the Company's strategy has been and will continue to be to concentrate on development drilling and/or the drilling of exploratory step out wells that are inherently less risky than drilling wild cat wells.

*Pursuit of Selective Complementary Acquisitions.* We seek to acquire long-lived producing properties with a high degree of operating control, or operators that are known to be competent in the area, that contain opportunities to profitably increase natural gas and crude oil reserves booked by the Company.

Our 2005 strategy is to focus on a disciplined approach to investment that balances our drilling effort between exploration opportunities and the development program, along with complimentary acquisition opportunities.

The preceding paragraphs, discussing our strategic pursuits and goals, contain forward-looking information. There can be no assurance that we will be successful in carrying out our business strategy or that our strategy will not change as we evaluate and pursue our business strategy.

#### Governmental Regulation

The Company's business and the natural gas industry in general are heavily regulated. The availability of a ready market for natural gas production depends on several factors beyond the Company's control. These factors include regulation of natural gas production, federal and state regulations governing environmental quality and pollution control, the amount of natural gas available for sale, the availability of adequate pipeline and other transportation and processing facilities and the marketing of competitive fuels. State and federal regulations generally are intended to prevent waste of natural gas, protect rights to produce natural gas between owners in a common reservoir and control contamination of the environment. Pipelines are subject to the jurisdiction of various federal, state, and local agencies.

The Company believes that it is in substantial compliance with such statutes, rules, regulations and governmental orders, although there can be no assurance that this is or will remain the case. Failure to comply with such laws and regulations can result in substantial penalties. The regulatory burden on the industry increases our cost of doing business and affects our profitability. Although we believe we are in substantial compliance with all applicable laws and regulations, such laws and regulations are frequently amended or reinterpreted so we are unable to predict the future cost or impact of complying with such laws and regulations.

The following discussion of the regulation of the United States natural gas industry is not intended to constitute a complete discussion of the various statutes, rules, regulations and environmental orders to which the Company's operations may be subject.

## Regulation of Oil and Natural Gas Exploration and Production

The Company's oil and natural gas operations are subject to various types of regulation at the federal, state and local levels. Prior to commencing drilling activities for a well, the Company (or its operating subsidiaries, operating entities or operating partners) must procure permits and/or approvals for the various stages of the drilling process from the applicable state and local agencies in the state in which the area to be drilled is located. Such permits and approvals include those for the drilling of wells, and such regulation includes maintaining bonding requirements in order to drill or operate wells and regulating the location of wells, the method of drilling and casing wells, the surface use and restoration of properties on which wells are drilled, the plugging and abandoning of wells and the disposal of fluids used in connection with operations. The Company's 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 and the density of wells which may be drilled and the unitization or pooling of natural gas properties. In this regard, some states allow the forced pooling or integration of tracts to facilitate exploration while other states rely primarily or exclusively on voluntary pooling of lands and leases. In areas where pooling is voluntary, it may be more difficult to form units, and therefore, more difficult to develop a project if the operator owns less than 100% of the leasehold. In addition, state conservation laws may establish maximum rates of production from oil and natural gas wells, generally prohibit the venting or flaring of natural gas and impose certain requirements regarding the ratability of production.

The effect of these regulations may limit the amount of oil and natural gas the Company can produce from its wells and may limit the number of wells or the locations at which the Company can drill. The regulatory burden on the oil and natural gas industry increases the Company's costs of doing business and, consequently, affects its profitability. Inasmuch as such laws and regulations are frequently expanded, amended and reinterpreted, the Company is unable to predict the future cost or impact of complying with such regulations.

## Natural Gas Marketing, Gathering, and Transportation

Federal legislation and regulatory controls have historically affected the price of the natural gas and the manner in which production is transported and marketed. Under the Natural Gas Act of 1938, the Federal Energy Regulatory Commission ("FERC") regulates the interstate sale for resale of natural gas and the transportation of natural gas in interstate commerce, although facilities used in the production or gathering of natural gas in interstate commerce are generally exempted from FERC jurisdiction. Effective January 1, 1993, the Natural Gas Wellhead Decontrol Act deregulated natural gas prices for all "first sales" of natural gas, which definition covers all sales of our own production. In addition, as part of the broad industry restructuring initiatives described below, the FERC has granted to all producers such as us a "blanket certificate of public convenience and necessity" authorizing the sale of gas for resale without further FERC approvals. As a result, all natural gas that we produce in the future may now be sold at market prices, subject to the terms of any private contracts that may be in effect.

Natural gas sales prices nevertheless continue to be affected by intrastate and interstate gas transportation regulation, because the prices that companies such as ours receive for our production are affected by the cost of transporting the gas to the consuming market. Through a series of comprehensive rulemakings, beginning with Order No.436 in 1985 and continuing through Order No.636 in 1992 and Order No.637 in 2000, the FERC has adopted regulatory changes that have significantly altered the transportation and marketing of natural gas. These changes were intended by the FERC to foster competition by, among other things, transforming the role of interstate pipeline companies from wholesale marketers of gas to the primary role of gas transporters, and by increasing the transparency of pricing for pipeline services. The FERC has also developed rules governing the relationship of the pipelines with their marketing affiliates, and implemented standards relating to the use of electronic data exchange by the pipelines to make transportation information available on a timely basis and to enable transactions to occur on a purely electronic basis.

In light of these statutory and regulatory changes, most pipelines have divested their gas sales functions to marketing affiliates, which operate separately from the transporter and in direct competition with all other merchants, and most pipelines have also implemented the large-scale divestiture of their gas gathering facilities to affiliated or non-affiliated companies. Interstate pipelines thus now generally provide unbundled, open and nondiscriminatory transportation and transportation-related services to producers, gas marketing companies, local distribution companies, industrial end users and other customers seeking such services. Sellers and buyers of gas have gained direct access to the particular pipeline services they need, and are better able to conduct business with a larger number of counterparties.

#### Environmental Regulations

The Company's operations are subject to numerous laws and regulations governing the discharge of materials into the environment or otherwise relating to environmental protection. Public interest in the protection of the environment has increased dramatically in recent years. The trend of more expansive and stricter environmental legislation and regulations could continue. To the extent laws are enacted or other governmental action is taken that restricts drilling or imposes environmental protection requirements that result in increased costs to the natural gas industry in general, the business and prospects of the Company could be adversely affected.

The nature of the Company business operations results in the generation of wastes that may be subject to the Federal Resource Conservation and Recovery Act ("RCRA") and comparable state statutes. The U.S. Environmental Protection Agency ("EPA") and various state agencies have limited the approved methods of disposal for certain hazardous and nonhazardous wastes. Furthermore, certain wastes generated by the Company's operations that are currently exempt from treatment as "hazardous wastes" may in the future be designated as "hazardous wastes," and therefore be subject to more rigorous and costly operating and disposal requirements.

The Comprehensive Environmental Response, Compensation and Liability Act ("CERCLA"), also known as the "Superfund" law, imposes liability, without regard to fault or the legality of the original conduct, on certain classes of persons who are considered to be responsible for the release of a "hazardous substance" into the environment. These persons include the present or past owners or operators of the disposal site or sites where the release occurred and the companies that transported or arranged for the disposal of the hazardous substances at the site where the release occurred. Under CERCLA, such persons may be subject to joint and several liabilities for the costs of cleaning up the hazardous substances that have been released into the environment, for damages to natural resources and for the costs of certain health studies. It is not uncommon for neighboring landowners and other third parties to file claims for personal injury and property damages allegedly caused by the release of hazardous substances or other pollutants into the environment. Furthermore, although petroleum, including natural gas and crude oil, is exempt from CERCLA, at least two courts have ruled that certain wastes associated with the production of crude oil may be classified as "hazardous substances" under CERCLA and thus such wastes may become subject to liability and regulation under CERCLA. State initiatives to further regulate the disposal of crude oil and natural gas wastes are also pending in certain states, and these various initiatives could have adverse impacts on our business.

Stricter standards in environmental legislation may be imposed on the industry in the future. For instance, legislation has been proposed in Congress from time to time that would reclassify certain exploration and production wastes as “hazardous wastes” and make the reclassified wastes subject to more stringent handling, disposal and clean-up restrictions. If such legislation were to be enacted, it could have a significant impact on our operating costs, as well as on the industry in general. Compliance with environmental requirements generally could have a materially adverse effect upon our capital expenditures, earnings or competitive position.

CERCLA and similar state laws impose liability, without regard to fault or the legality of the original conduct, on certain classes of persons that are considered to have contributed to the release of a “hazardous substance” into the environment. These persons include the owner or operator of the disposal site or sites where the release occurred and companies that disposed of or arranged for the disposal of the hazardous substances found at the site. Persons who are or were responsible for release of hazardous substances under CERCLA may be subject to joint and several liability for the costs of cleaning up the hazardous substances that have been released into the environment and for damages to natural resources, and it is not uncommon for neighboring landowners and other third parties to file claims for personal injury and property damage allegedly caused by the hazardous substances released into the environment.

The Company’s operations may be subject to the Clean Air Act (“CAA”) and comparable state and local requirements. Amendments to the CAA were adopted in 1990 and contain provisions that may result in the gradual imposition of certain pollution control requirements with respect to air emissions from the operations of the Company. The EPA and states have been developing regulations to implement these requirements. The Company may be required to incur certain capital expenditures in the next several years for air pollution control equipment in connection with maintaining or obtaining operating permits and approvals addressing other air emission-related issues.

The Federal Water Pollution Control Act (FWPCA or Clean Water Act) and resulting regulations, which are implemented through a system of permits, also govern the discharge of certain contaminants into waters of the United States. Sanctions for failure to comply strictly with the Clean Water Act are generally resolved by payment of fines and correction of any identified deficiencies. However, regulatory agencies could require us to cease construction or operation of certain facilities that are the source of water discharges.

Our operations are subject to local, state and federal laws and regulations to control emissions from sources of air pollution. Payment of fines and correction of any identified deficiencies generally resolve penalties for failure to comply strictly with air regulations or permits. Regulatory agencies could also require us to cease construction or operation of certain facilities that are air emission sources. We believe that we substantially comply with the emission standards under local, state, and federal laws and regulations.

#### Operating Hazards and Insurance

The Company’s exploration and production operations include a variety of operating risks, including the risk of fire, explosions, blowouts, craterings, pipe failure, casing collapse, abnormally pressured formations, and environmental hazards such as gas leaks, ruptures and discharges of toxic gas, the occurrence of any of which could result in substantial losses to the Company due to injury and loss of life, severe damage to and destruction of property, natural resources and equipment, pollution and other environmental damage, clean-up responsibilities, regulatory investigation and penalties and suspension of operations. The Company’s pipeline, gathering and distribution operations are subject to the many hazards inherent in the natural gas industry. These hazards include damage to wells, pipelines and other related equipment, and surrounding properties caused by hurricanes, floods, fires and other acts of God, inadvertent damage from construction equipment, leakage of natural gas and other hydrocarbons, fires and explosions and other hazards that could also result in personal injury and loss of life, pollution and suspension of operations.



Any significant problems related to its facilities could adversely affect the Company's ability to conduct its operations. In accordance with customary industry practice, the Company maintains insurance against some, but not all, potential risks; however, there can be no assurance that such insurance will be adequate to cover any losses or exposure for liability. The occurrence of a significant event not fully insured against could materially adversely affect the Company's operations and financial condition. The Company cannot predict whether insurance will continue to be available at premium levels that justify its purchase or whether insurance will be available at all.

### Competition

Competition in our primary producing areas is intense. Price, contract terms and quality of service, including pipeline connection times, distribution efficiencies and reliable delivery records, affect competition. In addition, there is tremendous competition within the United States to assemble an extensive acreage position, existing natural gas gathering and pipeline systems and storage fields. We actively compete against other companies with substantially larger financial and other resources.

The Company believes that its capabilities and the experience of its management and professional staff generally enable it to compete effectively. The Company encounters competition from numerous other oil and natural gas companies, drilling and income programs and partnerships in all areas of its operations, including drilling and marketing natural gas and obtaining desirable natural gas leases. Many of these competitors possess larger staffs and greater financial resources than the Company, which may enable them to identify and acquire desirable producing properties and drilling prospects more economically. The Company's ability to explore for oil and natural gas prospects and to acquire additional properties in the future depends upon its ability to conduct its operations, to evaluate and select suitable properties and to consummate transactions in this highly competitive environment. The Company competes with a number of other companies, which offer interests in drilling partnerships with a wide range of investment objectives and program structures. Competition for investment capital for both public and private drilling programs is intense. The Company also faces intense competition in the marketing of natural gas from competitors including other producers as well as marketing companies. Also, international developments and the possible improved economics of domestic natural gas exploration may influence other companies to increase their domestic oil and natural gas exploration. Furthermore, competition among companies for favorable prospects can be expected to continue, and it is anticipated that the cost of acquiring properties may increase in the future. Factors affecting competition in the natural gas industry include price, location, availability, quality and volume of natural gas. The Company believes that it can compete effectively in the oil and natural gas industry on each of the foregoing factors. Nevertheless, the Company's business, financial condition or results of operations could be materially adversely affected by competition.

### Employees

As of December 31, 2004, the Company had 6 employees, and 3 part-time consultants that dedicate over 25% of their time to the Company.

The Company's employees are not covered by a collective bargaining agreement. The Company considers relations with its employees to be excellent.

**Item 2. PROPERTIES.**

**Glossary of Oil and Gas Terms.**

Barrel: Equal to 42 U.S. gallons.

Barrels of oil equivalent (BOE) - Gas volume that is expressed in terms of its energy equivalent in barrels of oil, which is calculated as 6,000 cubic feet of gas equals 1 barrel of oil equivalent (BOE); or 42 U.S. gallons of oil at 40 degrees Fahrenheit.

Basin: A depressed sediment-filled area, roughly circular or elliptical in shape, sometimes very elongated. Regarded as a good area to explore for oil and gas.

BCF: One billion cubic feet of natural gas, or 1,000 mcf.

Field: A geographic region situated over one or more subsurface oil and gas reservoirs encompassing at least the outermost boundaries of all oil and gas accumulations known to be within those reservoirs vertically projected to the land surface.

License: Formal or legal permission to explore for oil and gas in a specified area.

MCF: One thousand cubic feet of natural gas. Natural gas is usually priced on an mcf basis, adjusted for BTU content.

Productive: Able to produce oil and/or gas.

Proved reserves: Estimated quantities of crude oil, condensate, natural gas, and natural gas liquids that geological and engineering data demonstrate with reasonable certainty to be commercially recoverable in the future from known reservoirs under existing conditions using established operating procedures and under current governmental regulations.

Proved undeveloped reserves: Economically recoverable reserves estimated to exist in proved reservoirs, which will be recovered from wells, drilled in the future.

Reserves: The estimated value of oil, gas and/or condensate, which is economically recoverable.

The Company has not filed reserve estimates with any federal agency.

Effective July 1, 2004, for accounting purposes, Teton sold its interest in Goloil. The chart below sets forth certain production data for the fiscal years ending December 31, 2002 and 2003, and for the period ending June 30, 2004, prior to such sale. Additional oil and gas disclosure can be found in Note 9 of the Financial Statements.

### PRODUCTION DATA

|  | 2004      | 2003      | 2002      |
|--|-----------|-----------|-----------|
| Total gross oil production, barrels    | 1,393,616 | 2,528,260 | 1,884,933 |
| Total gross gas production, MCF        | -         | -         | -         |
| Net oil production, barrel (1)         | 348,404   | 632,065   | 471,233   |
| Net gas production, MCF                | -         | -         | -         |
| Average oil sales price, \$/Bbl (2)    | \$ 18.98  | \$ 18.11  | \$ 15.62  |
| Average gas sales price, S/MCF         | -         | -         | -         |
| Average production cost per barrel (3) | \$ 16.12  | \$ 16.11  | \$ 13.32  |
| Gross productive wells                 |           |           |           |
| Oil                                    | 24.0      | 21.0      | 13.0      |
| Gas                                    | -         | -         | -         |
| Total                                  | 24.0      | 21.0      | 13.0      |
| Net productive wells                   |           |           |           |
| Gas                                    | -         | -         | -         |
| Total                                  | 12.0      | 10.5      | 6.5       |

(1) Net production and net well count is based on Teton's effective net interest as of the end of each year. Prior to August 2000 and after November 2002, Teton owned 100% of the effective net interest in Goltech.

(2) Average oil sales price is a combination of domestic (Russian) and export price.

(3) Excludes production payment to EUA.



(4) The following chart sets forth the number of productive wells and dry exploratory and productive wells drilled and completed during the last three fiscal years in the Goloil license area prior to the sale of Teton's interest in Goloil:

**NET WELLS DRILLED**

| Year Ended December 31,        | 2004       |            | 2003       |            | 2002       |            |
|--------------------------------|------------|------------|------------|------------|------------|------------|
|                                | Gross      | Net (1)    | Gross      | Net (1)    | Gross      | Net (1)    |
| <b>Number of Wells Drilled</b> |            |            |            |            |            |            |
| <b>Exploratory (Research)</b>  |            |            |            |            |            |            |
| Productive                     | -          | -          | -          | -          | -          | -          |
| Dry                            | -          | -          | -          | -          | -          | -          |
| <b>Total</b>                   | -          | -          | -          | -          | -          | -          |
| <b>Development</b>             |            |            |            |            |            |            |
| Productive                     | 3.0        | 1.5        | 7.0        | 3.5        | 6.0        | 3.0        |
| Dry                            | -          | -          | -          | -          | -          | -          |
| <b>Total</b>                   | <b>3.0</b> | <b>1.5</b> | <b>7.0</b> | <b>3.5</b> | <b>6.0</b> | <b>3.0</b> |

(1) Net well count is based on Teton's effective net interest as of the end of each year. Prior to August 2000, Teton owned 100% of the interest in Goltech. Subsequent to August 2000 our interest was reduced to 50%. Subsequent to November 2002, Teton's effective net interest in Goloil again became 100%.

**Proved and Producing Properties**

At December 31, 2004 the Company did not have any proved or producing properties.

**Developed And Undeveloped Acreage**

At December 31, 2004 the Company did not have any developed or undeveloped acreage.

The following table sets forth the total gross and net developed acres and total gross and net undeveloped acres of the Company as of March 15, 2005:

|                         | Gross | Net   |
|-------------------------|-------|-------|
| Total Undeveloped Acres | 6,300 | 1,575 |

Such undeveloped acreage is concentrated in western Colorado.

Our offices are located in Denver, Colorado. We lease our offices from an unaffiliated third party. The term of such lease is one year, and the lease expires in July 2005.

**Item 3. LEGAL PROCEEDINGS.**

Teton currently is not a party to any material legal proceedings.

**Item 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.**

No matters were submitted to a vote of our security holders during the fourth quarter of 2004.

**PART II****Item 5. MARKET FOR COMMON EQUITY AND RELATED STOCKHOLDERS MATTERS.**

Teton's common stock is listed and principally traded on the American Stock Exchange, under the symbol "TPE." Our common stock is also listed for trading on the Frankfurt Stock Exchange (Germany) under the symbol "TP9."

Prior to listing on the AMEX on May 6, 2003, our common stock was quoted on the OTC Bulletin Board under the symbol "TTPT" from November 27, 2001 to April 25, 2003 and then under the symbol "TTPE" from April 28, 2003 to May 5, 2003 as a result of a 1 for 12 reverse stock split.

The following table sets forth, on a per share basis, the range of high and low bid information for the common stock on the OTC Bulletin Board until May 5, 2003, and after May 5, 2003 the high and low closing price on the American Stock Exchange:

|                                       | High     | Low      |
|---------------------------------------|----------|----------|
| 2004 period                           |          |          |
| First quarter                         | \$ 5.24  | \$ 3.36  |
| Second quarter                        | \$ 4.00  | \$ 1.80  |
| Third quarter                         | \$ 2.55  | \$ 1.25  |
| Fourth quarter                        | \$ 1.85  | \$ 1.20  |
| 2003 period                           |          |          |
| First quarter                         | \$ 5.52* | \$ 3.36* |
| Second quarter as of May 5, 2003      | \$ 5.00* | \$ 4.10* |
| Second quarter commencing May 6, 2003 | \$ 5.40  | \$ 4.10  |
| Third quarter                         | \$ 4.58  | \$ 3.71  |
| Fourth quarter                        | \$ 5.58  | \$ 3.80  |

\*Represents quotations while the Company was listed on the OTC Bulletin Board. The quotations from the OTC Bulletin Board reflect inter-dealer prices without retail markup, markdown, or a commission, and may not necessarily represent actual transactions.

Holders: As of March 10, 2005, there were approximately 197 holders of record of Teton's common stock.

Dividends: Teton has not paid any dividends on its common stock since inception. Teton does not anticipate declaration or payment of any dividends at any time in the foreseeable future.

**Recent Issuances of Unregistered Securities**

During the fourth quarter, 8,451 unregistered shares of Teton's common stock were issued to the members of Teton's advisory board for services. The securities were issued in reliance on an exemption from registration provided in Section 4(2) of the Securities Act of 1933, as amended, based on the limited number of purchasers, their access to material information concerning the Company and their representations that they were acquiring the securities for investment.

**Equity Compensation Plan Information**

The following table sets forth information about our equity compensation plans at December 31, 2004:

| Plan category  | Number of securities to be issued upon exercise of outstanding options, warrants and rights<br>(a) | Weighted average exercise price of outstanding options, warrants and rights<br>(b) | Number of securities remaining available for future issuance<br>(c) |
|--|--|--|---|
| Equity compensation plans approved by security holders     | 1,999,037  | \$ 3.51  | 6,963   |
| Equity compensation plans not approved by security holders | 994,000  | \$ 3.60  | 0   |
| <b>Total</b>   | <b>2,993,037</b>   | <b>\$ 3.48</b>   | <b>6,963</b>  |

See Note 5 to the financial statements for discussion of options issued in 2004.

**Item 6. SELECTED FINANCIAL DATA.**

The following table sets forth selected financial data, derived from the financial statements, regarding Teton's financial position and results of operations as of the dates indicated. This selected financial data should be read in conjunction with our financial statements and notes to the financial statements.

|                                     | As of and for the Year Ended December 31, |                |                 |                |                |
|-------------------------------------|---|----------------|-----------------|----------------|----------------|
|                                     | 2004                                      | 2003           | 2002            | 2001           | 2000           |
| <b>Summary of Operations</b>        |   |                |                 |                |                |
| Loss from continuing operations     | \$ (5,193,281)                            | \$ (4,036,164) | \$ (10,191,307) | \$ (1,373,470) | \$ (2,825,767) |
| Discontinued operations, net of tax | 12,383,582                                | (1,598,680)    | (782,616)       | (284,138)      | (240,102)      |
| Net income (loss)                   | 7,190,301                                 | (5,634,844)    | (10,973,923)    | (1,657,608)    | (3,065,869)    |
| Income (loss) per share for:        |   |                |                 |                |                |
| Continuing operations               | \$ (.64)                                  | \$ (1.00)      | \$ (3.28)       | \$ (.05)       | \$ (.16)       |
| Discontinued operations             | 1.37                                      | (.23)          | (.25)           | (.01)          | (.01)          |
| Net income                          | .73                                       | (1.23)         | (3.53)          | (.06)          | (.17)          |
| <b>Balance Sheet</b>                |   |                |                 |                |                |
| Total assets                        | 17,611,565                                | 20,718,375     | 10,012,395      | 2,211,312      | 2,317,099      |
| Notes payable                       | --  | --             | --              | 844,210        | 1,425,000      |
| Cash dividends per common share     | --  | --             | --              | --             | --             |

**Item 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.**

The following discussion and analysis of our plan of operation should be read in conjunction with the financial statements and the related notes.

We have identified certain policies as critical to our business operations and the understanding of our results of operations. The impact and any associated risks related to these policies on our business operations is discussed throughout Management's Discussion and Analysis of Financial Condition and Results of Operations where such policies affect our reported and expected financial results.

## Overview

Teton Petroleum Company is an independent oil and gas exploration and production company which is currently focused on a drilling program in the Piceance Basin in western Colorado of 6,300 acres and a separate acreage play of up to 180,000 acres in North America. Teton's primary focus, until July 16, 2004 was the Russian Federation and former Commonwealth of Independent States ("CIS"). See "Sale of Goloil Interest" below. The Company, through its wholly owned subsidiary, Goltech, owned a 35.30% equity interest in Goloil. RussNeft (the Company's partner in Goloil) owned, until the sale, the remaining 64.70% of Goloil through two subsidiaries, McGrady and InvestPetrol. McGrady held 35.29% and InvestPetrol held 29.41% of the equity interests in Goloil. However, until Goltech and McGrady received the return of 100% of their capital investment in Goloil, they were each entitled to a 50% net profit in Goloil. During our ownership of Goloil, it was managed by a seven person management board on which we had two representatives. Pursuant to the existing agreements among Goloil's shareholders, Goltech and McGrady shared equally in capital expenditures, gross revenues, costs and expenses, until they received 100% return of their investments in Goloil. Limited Liability Company Energosoyuz-A ("EUA"), a wholly owned subsidiary of RussNeft, is the lessor of certain oil field facilities to Goloil pursuant to a Lease Agreement No. EST 160/000630 (the "EUA Lease Agreement") among EUA as lessor and Goloil as lessee dated as June 2000. EUA was also the recipient of a production payment ("Production Payment") consisting of 50% of Goloil's production (or at EUA's option, cash in lieu of such production). Between October 2003 through the effective date of the sale EUA took cash instead of oil under the Production Payment in the amount of approximately \$650,000 per month. In addition, Goloil had been selling its oil at a fixed price of 2,400 rubles per ton or \$11.50 per barrel and starting May 2004, 2,700 rubles per ton or \$12.74 per barrel. It is possible that a significant portion of such sales were made to or through one or more affiliates of RussNeft.

RussNeft, which was founded in the fall of 2002, is one of Russia's largest independent oil producers. In September 2003, RussNeft acquired a 64.70% equity interest in Goloil in a private transaction in which it purchased all of the ownership interests in McGrady and InvestPetrol, the other shareholders of Goloil. At that time, RussNeft also acquired EUA, the lessor of various wells and facilities to Goloil under the EUA Lease Agreement. In acquiring such interests, RussNeft became entitled to appoint a majority of the management board of Goloil and succeeded to EUA's interest in the Production Payment.

Financial highlights for the year ended December 31, 2004 include the following:

- Teton sold its share in Goloil and recorded a gain of \$13,086,761.
- Teton's net loss from continuing operations for the fourth quarter ended December 31, 2004 was \$905,832 compared to \$1,296,412 for the same period in 2004. Teton's net loss from continuing operations for the year ended December 31, 2004 was \$5,193,281 compared to \$4,036,164 for 2003.

During 2004 Teton's activities were focused in three areas:

- Negotiating and finalizing the sale of Goloil to RussNeft; and
- Evaluating and negotiating potential acquisitions of other producing oil properties in the United States, Russia and the CIS.
- Signing a Letter of Intent to acquire up to 180,000 acres in a North American oil and gas play.

### **Sale of Goloil Interest to RussNeft**

The sale of the Company's interest in Goloil received shareholder approval, at our annual meeting held July 16, 2004, and the sale closed on August 3, 2004, effective July 1, 2004 for accounting purposes. The purchase price for our 35.30% interest in Goloil was \$8,960,000 in cash, which was received during August 2004. Goloil also repaid advances made by the Company to Goloil totaling \$6,040,000. The advances were made to Goloil by the Company to finance our 50% share of Goloil's capital expenditures and currently bore interest at the rate of 8% per annum. The gross proceeds of the two transactions to the Company totaled \$15,000,000.

### **2005 Operational and Financial Objectives - Update**

During 2004, the Company actively sought to increase shareholder value by seeking to acquire both producing and non-producing properties that would provide for near-term cash flow and/or the ability to grow reserves and production, primarily through drilling operations in the United States, Russia and the CIS, where the Company itself will have the opportunity to jointly or fully operate the property. In particular, the Company elected to target properties in North America with existing production in the range of 400 to 600 barrels of oil equivalent per day and 2,000 barrels of oil equivalent per day in the former Soviet Union with upside potential from developmental drilling and other exploitation opportunities. Among the financial criteria for such acquisitions was that they generate positive cash flow and be accretive to the Company earnings within approximately one year. Over the past two years, the Company has evaluated over 300 projects. The Company announced the signing of a binding letter of intent in December 2004 and subsequently the signing of a definitive purchase agreement in January 2005 regarding up to 180,000 acres in North America. It is in the process of completing the due diligence on that acreage. In addition, the Company closed a separate acquisition in February 2005, in which it purchase a 25% interest in 6,300 acres in the Piceance Basin in Western Colorado. See subsequent events below.

Prior to August 2004 the Company emphasized acquisitions in Russia and the CIS. Recent developments in Russia have caused the Company to redirect the focus of its efforts, most recently, on opportunities in North America and specifically in the Rocky Mountains.

The Company's plans to pursue acquisitions means that it will incur due diligence and legal expenses, which will be capitalized if the Company successfully completes an acquisition. If an acquisition is not successful, such costs will be included in its general and administrative expenses. The Company is now devoting significant internal resources to evaluating acquisitions while also utilizing the services of outside technical, legal and accounting consultants.

### **Results of Operations 2004 Compared to 2003**

The Company has a net loss from continuing operations for the year ending December 31, 2004 of \$5,193,281 compared to a loss of \$4,036,164 for the prior year, which is an increase of \$1,157,117 primarily due to the increase in general and administrative expenses from \$3,920,791 for the year ending December 31, 2003 to \$5,332,291 for the year ending December 31, 2004. This is due to several reasons including:

- The Company pursued, but failed to close on, several acquisitions which resulted in the expensing of the various due diligence costs incurred on such acquisitions (\$409,000).
- The Company increased its payroll during the early part of 2004 as it increased its staffing levels to begin its investment and acquisition program (\$358,000).
- As part of their performance review for 2003, the Board paid out bonuses to senior management in the first quarter of 2004 (\$300,000).

- The Company began compensating outside Directors in cash and stock payments (\$140,000)

- The Company incurred significant legal, investor relations, accounting and other expenses in selling its interest in Goloil and in preparation of the related proxy statement in order to obtain shareholder approval of such sale (\$188,000).
- Since July of 2004 the Company has incurred severance and other one time costs as it reduces its staff, offices and other commitments (\$218,000).
- The Company opened a representative office in Moscow in December 2003 to better monitor its operations, as well as to establish a higher profile in the Russian oil industry and facilitate greater deal flow as it pursued acquisition opportunities in Russia and in other FSU states. Then, due to the Company's decision to exit Russia, as discussed above, such office was closed in December 2004 and the Company incurred closing costs which have been included in continuing operations at December 31, 2004 (\$70,000).

Other income in 2004 includes interest income from the cash balances maintained. The Company expects to continue to streamline its costs in the future, and, as of March 13, 2005, the Company has reduced its monthly overhead, exclusive of due diligence costs, to \$150,000 per month, and expects further adjustments as it refocuses its effort on projects in the U.S. Rocky Mountains.

#### Discontinued Operations 2004 Compared to 2003

See Note 2 to financial statements for a summary of the income (loss) from discontinued operations. The Company considered the sale of Goloil to be effective July 1, 2004. Accordingly, the operating activities of Goloil for the six months ended June 30, 2004 have been included in the Company's 2004 statement of operations as a net loss from discontinued operations. Goloil's operating revenues and expenses for six months of 2004 are less than 2003 because Teton has recorded a full year of operations for 2003. Goloil sold its production in 2004 at an average price of \$18.98 per barrel which approximates the \$18.11 price for oil sold in 2003. However, 2004 production was sold exclusively to the domestic and near abroad markets and not the export market which during 2004 were selling oil at a price substantially above the price received. Prior to September 30, 2003, Goloil had sold its oil for a blended oil price which included sales to the export market.

The \$13,086,761 gain includes the \$8,960,000 proceeds from the sale of Goloil stock, net of \$997,000 in expenses plus the elimination of approximately \$5.1 million in net liabilities included in the pro rata consolidation of Goloil as of June 30, 2004

#### Results of Operations 2003 Compared to 2002

The Company's net loss from continuing operations decreased from \$10,191,307 in 2002 to a net loss of \$4,036,164 in 2003. This was primarily due to the fact that general and administrative expenses decreased from \$4,744,952 in 2002 to \$3,920,791 in 2003, primarily due to a decrease of \$1,562,575 in fees paid to consultants for capital raising activities offset by increases in compensation to officers and employees (\$323,951) professional fees (\$109,146) travel and entertainment (\$193,773), and expenses related to marketing, advertising, and investor relations (\$167,987).

Financing charges recorded decreased from \$5,498,106 in 2002 to \$132,818 in 2003. In 2002, the Company recorded a \$4,715,000 non-cash financing charge as a result of warrants issued with debentures and in-the-money conversion features present at issuance.

#### Discontinued Operations 2003 Compared to 2002

See Note 2 to the financial statements for a summary of the loss from discontinued operations for 2003 and 2002. The loss from discontinued operations increased to \$1,598,680 for the year ending December 31, 2003 from \$782,616 for



the year ended December 31, 2002. Teton's share of Goloil's costs of sales and expenses increased 62.2%, which was slightly less than the increase in revenues. However, depreciation, depletion and amortization expense recorded for 2003 rose 250.1%, from \$451,930 to \$1,582,513, reflecting the capital expenditures incurred by Goloil as it developed its license.

### **Liquidity and Capital Resources**

The Company had a cash balance of \$17,433,424 at December 31, 2004 and a working capital surplus of \$17,103,015.

See subsequent events below for a discussion of the Company's purchase of 25% of the membership interest in Piceance Gas Resources, LLC from PGR. In addition to the cash purchase price of \$5.25 million, the Company estimates that its cash commitment to PGR for the year ending December 31, 2005 will total \$3,500,000. Such commitment includes the Company's share of the cost of a road and the drilling of eight wells. At this point in time, the Company anticipates utilizing the working capital of the Company to meet its commitment. However, the business plan for PGR Partners, LLC includes using commercial bank financing, when practical.

The Company has the working capital to complete the additional purchase of up to 180,000 acres in April 2005 (see subsequent events below) and to begin its evaluation of the prospects on such acreage.

The Company may require additional financing during 2006 for the anticipated capital programs for the two acquisitions or if the Company identifies other acquisitions that meet its investment criteria. Such additional financing may be debt or equity or a combination of both. See sources and uses of funds below.

### **Sources and Uses of Funds**

Historically, Teton's primary source of liquidity has been cash provided by equity offerings. Such offerings are expected to continue to play an important role in financing Teton's business for the foreseeable future. In addition, the Company is working to establish a borrowing facility with one or more international banks, most likely in the form of a revolving line of credit that will be used primarily for the acquisition of producing properties and for developmental drilling and other capital expenditures.

### **Cash Flows and Capital Expenditures**

During the year ended December 31, 2004 the Company used \$4,420,775 in its operating activities primarily to finance its efforts in respect of potential acquisitions and in respect of personnel costs. This amount compares to \$3,063,845 used in operating activities in 2003.

During 2004, the Company received the reimbursement of advances totaling \$6,040,000 pursuant to its agreement with RussNeft and, net of expenses and taxes, \$7,963,450 from the sale of Goloil.

During 2004, the Company received \$499,998 from the sale of preferred stock. The increase in cash flows from financing activities from discontinued operations represents amounts advanced by RussNeft to Goloil. As discussed above, such advances will be eliminated now that the sale of Goloil has been completed.

### **Income Taxes, Net Operating Losses and Tax Credits**

While the Company will realize a U.S. tax gain from sale of discontinued operations of approximately \$12.0 million, after utilization of NOL and current year operating losses, Teton will not incur a tax liability. At December 31, 2004, after the gain on sale, the Company has a remaining net operating loss for U.S. income tax purposes of \$11,800,000. Such net operating loss is subject to U.S. Internal Revenue Code Section 382 limitations. As of November 1, 2004 utilization of the NOL is limited to approximately \$900,000 per annum.

The Company has established a valuation allowance for deferred taxes that reduces its net deferred tax assets as management currently believes that these losses will not be utilized in the near term. The allowance recorded was \$4.6 million and \$7.2 million for 2004 and 2003 respectively. The Company reduced the valuation allowance in 2004 by approximately \$2.6 million due to the utilization of net operating loss carryforwards.

### **Subsequent Events**

On January 5, 2005 the Company entered into a definitive purchase and sale agreement for the acquisition of certain oil and gas leases covering up to 180,000 acres in North America. The closing of the transaction is subject to the satisfactory results of a due diligence investigation and other conditions. The transaction is currently pending and the terms are being kept confidential subject to a request for confidential treatment previously filed with the Securities and Exchange Commission. The Company paid a nonrefundable deposit of \$25,000 in December upon signing a letter of intent. Earnest money of \$322,000 was paid in January upon signing the purchase and sale agreement. The balance due in cash, stock and warrants will be paid at closing. The Company expects to close the transaction on or before April 15, 2005.

On February 15, 2005, in a second acquisition, the Company signed a membership interest purchase agreement with PGR Partners, LLC ("PGR") whereby the Company acquired 25% of the membership interest in Piceance Gas Resources, LLC, a Colorado limited liability company ("Piceance LLC"). Piceance LLC owns certain oil and gas rights and leasehold assets covering approximately 6,300 acres in the Piceance Basin in Western Colorado. The properties owned by Piceance LLC carry a net revenue interest of 78.75%.

The purchase price for the membership interest in Piceance LLC was \$5.25 million in cash, the issuance of 450,000 unregistered shares of our common stock, and the issuance of warrants to purchase 200,000 shares of our common stock, exercisable for a period of five years at an exercise price of \$2.00 per share. Pursuant to the terms of the operating agreement, the Company is obligated to fund its share of the construction of a road on the leased area and eight wells to be drilled during 2005.

On February 22, 2005, Mr. Cooper resigned as executive chairman of the Company. Mr. Cooper will remain on the Company's Board and will stand for reelection at the Company's upcoming annual meeting in May. In addition, Mr. Cooper will remain a consultant to the Company. On February 22, 2005, our Board elected James J. Woodcock, an outside director, as non-executive chairman of the Company.

**Item 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISKS.**

Market risk is the potential loss arising from adverse changes in market rates and prices, such as foreign currency exchange and interest rates and commodity prices. As of August, 2004, when the Company sold its interest in Goloil, the Company is no longer exposed to foreign currency exchange risk.

Currently, the Company is not involved in any hedge contracts, although we may consider hedge agreements in the future to manage the exposure to commodity price risk.

20

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**Item 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA**

**Consolidated Financial Statements  
and  
Independent Auditors' Report  
December 31, 2004 and 2003**

21

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**TETON PETROLEUM COMPANY**

Table of Contents

|  | <b>Page</b> |
|--|-------------|
| Report of Independent Registered Public Accounting Firm              | F - 1       |
| Consolidated Financial Statements                                    |             |
| Consolidated Balance Sheets  | F - 2       |
| Consolidated Statements of Operations and Comprehensive Loss         | F - 3       |
| Consolidated Statements of Changes in Stockholders' (Deficit) Equity | F - 4       |
| Consolidated Statements of Cash Flows                                | F - 5       |
| Notes to Consolidated Financial Statements                           | F - 9       |

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**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

Board of Directors and Stockholders  
Teton Petroleum Company  
Denver, Colorado

We have audited the accompanying consolidated balance sheets of Teton Petroleum Company and subsidiary as of December 31, 2004 and 2003, and the related consolidated statements of operations and comprehensive loss, changes in stockholders' (deficit) equity and cash flows for each of the years in the three year period ended December 31, 2004. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Teton Petroleum Company and subsidiary as of December 31, 2004 and 2003, and the results of their operations and their cash flows for each of the years in the three year period ended December 31, 2004 in conformity with accounting principles generally accepted in the United States of America.

/s/Ehrhardt Keefe Steiner & Hottman PC  
Ehrhardt Keefe Steiner & Hottman PC

Denver, Colorado  
March 4, 2005

## TETON PETROLEUM COMPANY

**Consolidated Balance Sheets**  
**December 31, 2004 and 2003**

|   | December 31,         |                      |
|---|----------------------|----------------------|
|   | 2004                 | 2003                 |
| <b>Assets</b>   |                      |                      |
| <b>Current assets</b>   |                      |                      |
| Cash  | \$ 17,433,424        | \$ 7,515,994         |
| Current assets of discontinued operations   | -                    | 1,615,365            |
| Prepaid expenses and other assets   | 100,917              | 95,693               |
| <b>Total current assets</b>   | <b>17,534,341</b>    | <b>9,227,052</b>     |
| <b>Non-current assets</b>   |                      |                      |
| Non-current assets of discontinued operations   | -                    | 11,473,139           |
| Deposits  | 25,000               | -                    |
| Fixed assets, net of accumulated depreciation of \$12,426 and \$1,046   | 52,224               | 18,184               |
| <b>Total non-current assets</b>   | <b>77,224</b>        | <b>11,491,323</b>    |
| <b>Total assets</b>   | <b>\$ 17,611,565</b> | <b>\$ 20,718,375</b> |
| <b>Liabilities and Stockholders' Equity</b>   |                      |                      |
| <b>Current liabilities</b>  |                      |                      |
| Accounts payable and accrued liabilities  | \$ 411,745           | \$ 376,429           |
| Current liabilities of discontinued operations  | -                    | 10,010,310           |
| <b>Total current liabilities</b>  | <b>411,745</b>       | <b>10,386,739</b>    |
| <b>Non-current liabilities</b>  |                      |                      |
| Discontinued operations   | -                    | 126,500              |
| <b>Total non-current liabilities</b>  | <b>-</b>             | <b>126,500</b>       |
| <b>Total liabilities</b>  | <b>411,745</b>       | <b>10,513,239</b>    |
| <b>Commitments</b>  |                      |                      |
| <b>Stockholders' equity</b>   |                      |                      |
| Series A convertible preferred stock, \$.001 par value, 25,000,000 shares authorized, 281,460 and 618,231 issued and outstanding at December 31, 2004 and 2003. Liquidation preference at December 31, 2004 and 2003 of \$1,248,838 and \$2,689,305 | 281                  | 618                  |
| Common stock, \$.001 par value, 250,000,000 shares authorized, 9,130,257 shares issued and outstanding at December 31, 2004 and 8,584,068 shares issued and outstanding at December 31, 2003  | 9,130                | 8,584                |
| <b>Additional paid-in capital</b>   | <b>37,657,686</b>    | <b>37,073,366</b>    |



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|  |               |               |
|--|---------------|---------------|
| Unamortized preferred stock dividends      | -             | (118,610)     |
| Accumulated deficit                        | (20,467,277)  | (27,657,578)  |
| Foreign currency translation adjustment    | -             | 898,756       |
| Total stockholders' equity                 | 17,199,820    | 10,205,136    |
| Total liabilities and stockholders' equity | \$ 17,611,565 | \$ 20,718,375 |

See notes to consolidated financial statements.

F - 2

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## TETON PETROLEUM COMPANY

## Consolidated Statements of Operations and Comprehensive Loss

|   | For the Years Ended December 31, |              |              |
|---|----------------------------------|--------------|--------------|
|   | 2004                             | 2003         | 2002         |
| Costs and expenses:   |                                  |              |              |
| General and administrative  | \$ 5,332,991                     | \$ 3,920,791 | \$ 4,744,952 |
| Total costs and expenses  | 5,332,991                        | 3,920,791    | 4,744,952    |
| Loss from operations  | (5,332,991)                      | (3,920,791)  | (4,744,952)  |
| Other income (expense)  |                                  |              |              |
| Other income  | 139,710                          | 17,445       | 51,751       |
| Financing charges   | -                                | (132,818)    | (5,498,106)  |
| Total other income (expense)  | 139,710                          | (115,373)    | (5,446,355)  |
| Loss from continuing operations   | (5,193,281)                      | (4,036,164)  | (10,191,307) |
| Discontinued operations, net of tax   | 12,383,582                       | (1,598,680)  | (782,616)    |
| Net income (loss)   | 7,190,301                        | (5,634,844)  | (10,973,923) |
| Imputed preferred stock dividends for inducements and beneficial conversion charges | (521,482)                        | (2,780,693)  | --           |
| Preferred stock dividends   | (105,949)                        | --           | --           |
| Net income (loss) applicable to common shares                                       | 6,562,870                        | (8,415,537)  | (10,973,923) |
| Other comprehensive income (loss), net of tax effect of exchange rates              |                                  |              | (898,756)    |
| )   |                                  |              | 168,256      |
| )   |                                  |              | (140,773)    |
| Comprehensive (loss) income   |                                  |              | 5,664,114    |
| \$  |                                  |              | (8,247,281)  |
| )   |                                  |              | (11,114,696) |
| )   |                                  |              |              |
| Basic and diluted weighted average common shares outstanding                        |                                  |              |              |

|  |           |
|--|-----------|
|  | 9,028,967 |
|  | 6,840,303 |
|  | 3,105,325 |
| Basic and diluted loss per common share for continuing operations                              |           |
| \$   | (0.64)    |
| )  |           |
| \$   | (1.00)    |
| )  |           |
| \$   | (3.28)    |
| )  |           |
| Basic and diluted weighted average income (loss) per common shares for discontinued operations |           |
| \$   | 1.37      |
| \$   | (0.23)    |
| )  |           |
| \$   | (0.25)    |
| )  |           |
| Basic and diluted income (loss) per common share   |           |
| \$   | 0.73      |
| \$   | (1.23)    |
| )  |           |
| \$   | (3.53)    |
| )  |           |

See notes to consolidated financial statements.

## TETON PETROLEUM COMPANY

## Consolidated Statements of Changes in Stockholders' (Deficit) Equity

|   | Preferred Stock |        | Common Stock |          | Additional<br>Paid-in<br>Capital | Unamortized<br>Preferred Stock<br>Dividends | Foreign Currency<br>Translation<br>Adjustment |
|---|-----------------|--------|--------------|----------|----------------------------------|---|---|
|   | Shares          | Amount | Shares       | Amount   |                                  |   |   |
| Balance -<br>December 31,<br>2001   | -               | \$ -   | 2,374,046    | \$ 2,374 | \$ 9,792,722                     | \$ -  | 871,273                                       |
| Common<br>stock issued<br>for cash  | -               | -      | 1,223,737    | 1,224    | 3,332,236                        | -   | -   |
| Common<br>stock<br>subscriptions<br>paid in 2003  | -               | -      | 712,045      | 712      | 1,938,898                        | -   | -   |
| Common<br>stock and<br>warrants<br>issued for<br>services                                       | -               | -      | 221,198      | 221      | 836,905                          | -   | -   |
| Common<br>stock issued<br>for<br>conversion of<br>convertible<br>debentures                     | -               | -      | 1,758,494    | 1,758    | 5,353,231                        | -   | -   |
| Warrants<br>issued and<br>in-the-money<br>conversion<br>feature on<br>convertible<br>debentures | -               | -      | -            | -        | 4,557,845                        | -   | -   |
| Warrants<br>issued with<br>notes payable  | -               | -      | -            | -        | 150,016                          | -   | -   |
| Warrants<br>issued in<br>connection<br>with<br>extensions on<br>notes payable                   | -               | -      | -            | -        | 203,362                          | -   | -   |
| Net loss  | -               | -      | -            | -        | -                                | -   | -   |
| Foreign<br>currency   | -               | -      | -            | -        | -                                | -   | (140,773)                                     |

|   |             |         |           |       |            |             |         |
|---|-------------|---------|-----------|-------|------------|-------------|---------|
| translation adjustment  |             |         |           |       |            |             |         |
| Balance - December 31, 2002   | -           | -       | 6,289,520 | 6,289 | 26,165,215 | -           | 730,500 |
| Common stock issued for cash - net of commissions of \$98,100                                   | -           | -       | 437,012   | 437   | 1,091,463  | -           | -       |
| Common stock issued for settlement of accounts payable and accrued liabilities                  | -           | -       | 79,793    | 80    | 219,920    | -           | -       |
| Options issued to advisory board and common stock issued for services                           | -           | -       | 1,035     | 1     | 97,901     | -           | -       |
| Warrants issued with notes payable  | -           | -       | -         | -     | 110,170    | -           | -       |
| Preferred stock issued for cash, net of commissions of \$473,838 (cash) and \$99,168 (non-cash) | 2,226,680   | 2,226   | -         | -     | 9,110,830  | -           | -       |
| Preferred stock converted to common stock   | (1,645,099) | (1,645) | 1,776,708 | 1,775 | (131)      | -           | -       |
| Preferred stock issued in exchange for notes payable and accrued interest of \$9,426            | 36,650      | 37      | -         | -     | 159,389    | -           | -       |
|   | -           | -       | -         | -     | 1,182,452  | (1,182,452) | -       |

|  |           |        |           |       |             |           |  |         |
|--|-----------|--------|-----------|-------|-------------|-----------|--|---------|
| In-the-money conversion feature charges to be amortized  |           |        |           |       |             |           |  |         |
| Amortization of in-the-money conversion feature charges  | -         | -      | -         | -     | (1,063,842) | 1,063,842 |  | -       |
| Net loss   | -         | -      | -         | -     | -           | -         |  | -       |
| Foreign currency translation adjustment  | -         | -      | -         | -     | -           | -         |  | 168,256 |
| Balance - December 31, 2003  | 618,231   | \$ 618 | 8,584,068 | 8,583 | 37,073,366  | (118,610) |  | 898,756 |
| Common stock issued for settlement of accrued liabilities                                      | -         | -      | 13,750    | 14    | 58,686      | -         |  | -       |
| Common stock issued for services   | -         | -      | 32,175    | 33    | 101,297     | -         |  | -       |
| Warrants issued for services   | -         | -      | -         | -     | 149,061     | -         |  | -       |
| Preferred stock issued for cash, net of commissions of \$50,000 (cash) and \$22,863 (non-cash) | 126,436   | 126    | -         | -     | 499,872     | -         |  | -       |
| Preferred stock converted to common stock  | (463,207) | (463)  | 500,264   | 500   | (37)        | -         |  | -       |
| Amortization of Preferred Stock dividends  | -         | -      | -         | -     | (118,610)   | 118,610   |  | -       |
| Preferred stock dividends  | -         | -      | -         | -     | (105,949)   | -         |  | -       |

|  |            |     |              |          |               |      |           |
|--|------------|-----|--------------|----------|---------------|------|-----------|
| Foreign<br>currency<br>translation<br>adjustment | -          | -   | -            | -        | -             | -    | (898,756) |
| Net income<br>for year                           | -          | -   | -            | -        | -             | -    | -         |
| Balance -<br>December 31,<br>2004                | 281,460 \$ | 281 | 9,130,257 \$ | 9,130 \$ | 37,657,686 \$ | - \$ | - \$      |

See notes to consolidated financial statements.

F - 4

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**TETON PETROLEUM COMPANY**

**Consolidated Statements of Cash Flows**

For the Years Ended December 31,

|   | 2004      | 2003        | 2002        |
|---|-----------|-------------|-------------|
| Cash flows from operating activities  |           |             |             |
| Net income (loss)   |           |             |             |
| \$  | 7,190,301 |             |             |
| \$  |           | (5,634,844  |             |
| )   |           |             |             |
| \$  |           | (10,973,923 |             |
| )   |           |             |             |
| Adjustments to reconcile net income (loss) to net cash used in operating activities |           |             |             |
| Depreciation, depletion, and amortization   |           |             | 11,380      |
|   |           |             | 1,046       |
|   |           |             | -           |
| Gain on sale of discontinued operations   |           |             | (13,086,761 |
| )   |           |             |             |
|   |           |             | -           |
|   |           |             | -           |
| Stock based compensation for variable plan warrants                                 |           |             | -           |
|   |           |             | -           |
|   |           |             | -           |
| Stock and stock options issued for services and interest                            |           |             | -           |
|   |           |             | 107,128     |
|   |           |             | -           |



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|  |           |
|--|-----------|
| Warrants issued for notes payable extensions         | -         |
|  | 110,170   |
|  | 46,582    |
| Stock and warrants issued for services               | 250,390   |
|  | -         |
|  | 837,126   |
| Debentures issued for services                       | -         |
|  | -         |
|  | 267,500   |
| Amortization of debenture and note payable discounts | -         |
|  | -         |
|  | 5,331,412 |
| Changes in assets and liabilities                    |           |
| From discontinued operations                         | 1,149,609 |
|  | 2,045,001 |
|  | (929,969) |
| )  |           |
| Prepaid expenses and other assets                    | (5,224)   |
| )  |           |
|  | (4,247)   |
| )  |           |
|  | (57,446)  |
| )  |           |
| Accounts payable and accrued liabilities             | 69,530    |
|  | 311,901   |
|  | 290,131   |

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|   |             |
|---|-------------|
| )   | (11,611,076 |
|   | 2,570,999   |
|   | 5,785,336   |
| Net cash used in operating activities                           |             |
| )   | (4,420,775  |
| )   | (3,063,845  |
| )   | (5,188,587  |
| Cash flows from investing activities                            |             |
| Proceeds from sale of discontinued operations                   |             |
|   | 7,963,450   |
|   | -           |
|   | -           |
| Repayments of loan from discontinued operating entity           |             |
|   | 6,040,000   |
|   | -           |
|   | -           |
| Increase in deposits  |             |
| )   | (25,000     |
|   | -           |
|   | -           |
| Increase in fixed asset additions                               |             |
| )   | (45,420     |
| )   | (20,684     |
|   | -           |
| Increase in non-current assets of discontinued operating entity |             |
| )   | (2,988,882  |
|   | (7,072,462  |

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|   |  |             |
|---|--|-------------|
| ) |  |             |
| ) |  | (3,222,349) |
|   | Net cash used in investing activities                                      |             |
|   |  | 10,944,148  |
| ) |  | (7,093,146) |
| ) |  | (3,222,349) |
|   | Cash flows from financing activities                                       |             |
|   | From discontinued operations   |             |
|   |  | 3,258,378   |
|   |  | 4,470,984   |
|   |  | 2,178,525   |
|   | Proceeds from stock subscription   |             |
|   |  | -           |
|   |  | 1,939,610   |
|   |  | -           |
|   | Proceeds from issuance of stock, net of \$50,000 and \$473,838 commissions |             |
|   |  | 499,998     |
|   |  | 10,251,924  |
|   |  | 3,333,460   |
|   | Proceeds from issuance of convertible debentures                           |             |
|   |  | -           |
|   |  | -           |
|   |  | 4,143,643   |
|   | Proceeds from notes payable  |             |
|   |  | -           |
|   |  | 628,750     |
|   |  | 300,000     |
|   | Payments on notes payable  |             |
|   |  | -           |
| ) |  | (478,750)   |

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|   |            |
|---|------------|
|   | (894,210   |
| )   |            |
| Dividends                                 | (81,463    |
| )   |            |
|   | -          |
|   | -          |
| Net cash provided by financing activities | 3,676,913  |
|   | 16,812,518 |
|   | 9,061,418  |
| Effect of exchange rates                  | (282,856   |
| )   |            |
|   | 168,256    |
|   | (140,773   |
| )   |            |
| Net increase in cash                      | 9,917,430  |
|   | 6,823,783  |
|   | 509,709    |
| Cash - beginning of year                  | 7,515,994  |
|   | 692,211    |
|   | 182,502    |
| Cash - end of year                        | 17,433,424 |
| \$  | 7,515,994  |
| \$  | 692,211    |
| \$  | 182,502    |

(Continued on the following page.)

See notes to consolidated financial statements.



**TETON PETROLEUM COMPANY****Consolidated Statements of Cash Flows**

(Continued from the previous page.)

Supplemental disclosure of cash flow information:

| Cash paid for: |    | Interest |
|----------------|----|----------|
| 2004           | \$ | --       |
| 2003           | \$ | 18,202   |
| 2002           | \$ | 120,008  |

Supplemental disclosure of non-cash activity:

During the year ended December 31, 2004, the Company had the following transactions:

The Company has issued warrants to consultants for services valued at \$149,061.

13,750 shares of common stock were issued for the settlement of accrued liabilities at December 31, 2003 valued at \$58,700.

The Company has issued 32,175 shares of common stock for services to consultants and outside directors valued at \$101,329.

Approximately \$1,317,000 of capital expenditures for discontinued operations were included in current liabilities of discontinued operations at June 30, 2004 and approximately \$1,786,000 of capital expenditures were in accounts payable at December 31, 2003 for a decrease during the six months ended June 30, 2004 of \$469,000.

Conversion of 463,207 shares of preferred stock, plus dividends of 37,057 shares converted into 500,264 shares of common stock.

The Company accrued dividends to preferred stockholders of \$24,486 at December 31, 2004.

See notes to consolidated financial statements.

**TETON PETROLEUM COMPANY**

**Consolidated Statements of Cash Flows**

(Continued from the previous page.)

During the year ended December 31, 2003, the Company had the following transactions:

128,700 warrants issued with debt and valued at \$110,170 were initially recorded as a discount on the note payable. At December 31, 2003, the full amount of the discount had been amortized as financing costs.

79,793 shares of common stock were issued for settlement of accounts payable and accrued liabilities valued at \$220,000.

The Company issued 30,000 non-qualified options to advisory board members valued at \$94,702.

The Company issued 1,035 shares of common stock for services valued at \$3,201.

The Company has accrued a liability for \$46,968 related to the obligation to issue 57,420 warrants to a consultant for capital raising services.

12,000 preferred shares were issued to consultants for services valued at \$52,200 related to capital raising.

Approximately \$1,785,000 of capital expenditures for oil and gas properties were included in current liabilities of discontinued operations at December 31, 2003.

(Continued on the following page.)

See notes to consolidated financial statements.

**TETON PETROLEUM COMPANY**

**Consolidated Statements of Cash Flows**

(Continued from the previous page.)

During 2002, the Company had the following transactions:

In exchange for the extension of principal payments on four notes payable, the Company modified expiration dates of certain warrants previously held by the note holders and issued an additional 10,416 such warrants. The fair value of the modification of the warrants totaled \$46,582 and has been recorded as financing costs.

A note payable of \$250,000 was converted into a convertible debenture with 83,333 warrants also being issued under the same terms of the Company's private placement offering of convertible debentures.

1,647,881 warrants were issued with convertible debentures valued at \$811,559 were initially recorded as a discount on the debentures. At December 31, 2002, the full amount of the discount had been amortized as financing costs.

In-the-money conversion features on convertible debt valued at \$3,746,285 were recognized as financing costs.

The Company issued 143,678 warrants in connection with related party notes payable of \$450,000 and \$50,000. The warrants were valued at \$156,781 and recorded as financing costs.

\$267,500 of convertible debentures with 89,167 warrants valued at \$14,250 for a total amount of \$281,750 were issued for consulting services.

41,667 warrants issued with a note payable valued at \$150,016 were initially recorded as a discount on the note payable. At December 31, 2002 the full discount had been amortized and recorded as financing costs.

\$4,661,143 of debentures and accrued interest of \$227,075 were converted into 1,758,494 shares of stock with \$466,771 being paid as a premium at conversion and recorded as financing costs.

221,198 shares of stock were issued to consultants for services valued at \$607,790.

133,333 warrants were issued to consultants for services valued at \$215,086.

Approximately \$1,142,000 of capital expenditures for oil and gas properties were included in current liabilities from discontinued operations at December 31, 2002.

During the fourth quarter of 2002, the Company received \$1,939,610 of stock subscriptions receivable for 712,045 shares of stock. The cash for these subscriptions was paid during the first quarter of 2003.

See notes to consolidated financial statements.



**TETON PETROLEUM COMPANY**

**Notes to Consolidated Financial Statements  
For The Years Ended December 31, 2004, 2003 and 2002**

**Note 1 - Description of Business and Summary of Significant Accounting Policies**

Teton Petroleum Company (the Company) is an oil and gas exploration and production company whose focus, prior to July 1, 2004, was the Russian Federation through ownership of a 35.30% interest in ZAO Goloil, a Russian closed joint-stock company ("ZAO Goloil"). The Company sold all of its interest in Goloil effective July 1, 2004 (see Note 2 to financial statements). Since the sale of ZAO Goloil, the Company has focused primarily on acquiring oil and gas prospects and properties in North America. See Note 8, Subsequent Events.

The exploration and development of oil and gas reserves involves significant financial risks. The ability of the Company to meet its obligations and commitments under the terms and conditions of its agreements and carry out its planned exploration activities is dependent upon continued financial support from its stockholders, the ability to develop economically recoverable reserves, and its ability to obtain necessary financing to complete development of the reserves.

The United States dollar is the principal currency of the Company's business and, accordingly, these consolidated financial statements are expressed in United States dollars.

**Discontinued Operations and Principles of Consolidation**

See Note 2 for a summary of the income (loss) from discontinued operations. The Company considers the sale of Goloil to be effective July 1, 2004 for accounting purposes. Accordingly the operating activities of ZAO Goloil for the six months ended June 30, 2004 and the years ended December 31, 2003 and 2002 have been included in the results from discontinued operations.

The accompanying consolidated financial statements include the accounts of Teton Petroleum Company and through June 30, 2004, its wholly owned subsidiary, Goltech Petroleum, LLC ("Goltech"). All intercompany accounts and transactions have been eliminated in consolidation.

During 2002, the Company owned a 50% interest in Goltech, which had a 70.59% interest in ZAO Goloil. Accordingly ZAO Goloil was consolidated into Goltech and the Company reflected its 50% share of Goltech. As of December 31, 2002, the other 50% member of Goltech relinquished their ownership interest in exchange for a 35.295% direct ownership interest in ZAO Goloil. The audited financial statements as of June 30, 2004, December 31, 2003 and 2002, as is customary in the oil and gas industry, reflect a pro-rata consolidation of the Company's interest in ZAO Goloil (a Russian Company) through its wholly owned subsidiary Goltech. Due to the sale of ZAO Goloil, the pro-rata consolidated amounts have been reclassified as assets, liabilities and included in the results from discontinued operations.

**TETON PETROLEUM COMPANY**

**Notes to Consolidated Financial Statements  
For The Years Ended December 31, 2004, 2003 and 2002**

**Note 1 - Description of Business and Summary of Significant Accounting Policies (continued)**

Use of Estimates

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

Cash and Cash Equivalents

The Company considers all highly liquid instruments purchased with an original maturity of three months or less to be cash equivalents. The Company continually monitors its positions with, and the credit quality of, the financial institutions it invests with. As of the balance sheet date, the Company had no cash equivalents.

Revenue Recognition

The Company recognizes oil sales revenue at the point in time oil quantities have been delivered to purchasers.

F - 10

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**TETON PETROLEUM COMPANY**

**Notes to Consolidated Financial Statements  
For The Years Ended December 31, 2004, 2003 and 2002**

**Note 1 - Description of Business and Summary of Significant Accounting Policies (continued)**

Comprehensive Income

Comprehensive income is defined as the change in equity during a period from transactions and other events from non-owner sources. Comprehensive income is the total of net income or loss and other comprehensive income or loss. The effect of foreign currency exchange rates currently is the Company's only item, which constitutes comprehensive income or loss.

Oil and Gas Properties

The Company uses the successful efforts method of accounting for oil and gas producing activities. Costs to acquire mineral interests in oil and gas properties, to drill and equip exploratory wells that find proved reserves, and to drill and equip development wells are capitalized. Costs to drill exploratory wells that do not find proved reserves, geological and geophysical costs, and costs of carrying and retaining unproved properties are expensed. The Company also evaluates costs capitalized for exploratory wells, and if proved reserves cannot be determined within one year from drilling exploration wells, those costs are written-off and recorded as an expense.

Unproved oil and gas properties that are individually significant are periodically assessed for impairment of value, and a loss is recognized at the time of impairment by providing an impairment allowance. Other unproved properties are amortized based on the Company's experience of successful drilling and average holding period. Currently the Company holds no unproved properties.

Capitalized costs of producing oil and gas properties, after considering estimated dismantlement and abandonment costs and estimated salvage values, are depreciated and depleted by the unit-of-production method. Significant development projects are excluded from the depletion calculation prior to assessment of the existence of proven reserves that are ready for commercial production. Support equipment and other property and equipment are depreciated over their estimated useful lives.

On the sale or retirement of a complete unit of a proved property, the cost and related accumulated depreciation, depletion, and amortization are eliminated from the property accounts, and the resulting gain or loss is recognized. On the retirement or sale of a partial unit of proved property, the cost is charged to accumulated depreciation, depletion, and amortization with a resulting gain or loss recognized in income based on the amount of proceeds.

On the sale of an entire interest in an unproved property for cash or cash equivalent, gain or loss on the sale is recognized, taking into consideration the amount of any recorded impairment if the property had been assessed individually. If a partial interest in an unproved property is sold, the amount received is treated as a reduction of the cost of the interest retained.

**TETON PETROLEUM COMPANY**

**Notes to Consolidated Financial Statements  
For The Years Ended December 31, 2004, 2003 and 2002**

**Note 1 - Description of Business and Summary of Significant Accounting Policies (continued)**

Oil and Gas Properties (continued)

Prior to July 1, 2004, all of the Company's oil and gas assets were held in one cost center located in Siberia, Russia. The Russian Federation (RF) has performed substantial exploration efforts on properties on which the Company has received successful tenders for future exploration and development. As a result, those areas accepted under tender by the RF are known to contain proved reserves and the Company's efforts are focused on further development of such reserves.

The net carrying value of the Company's oil and gas properties was limited to an estimated net recoverable amount. The net recoverable amount is based on undiscounted future net revenues and is determined by applying factors based on historical experience and other data such as primary lease terms of properties and average holding periods. If it is determined that the net recoverable value is less than the net carrying value of the oil and gas properties, any impairment is charged to operations.

Inventories

Inventory includes extracted oil physically in the pipeline prior to delivery for sale and oil held by third parties valued at the cost of development. Inventory also includes various supplies and spare parts and is valued at cost using the weighted average method.

Property and Equipment

Property and equipment is stated at cost. Depreciation is provided utilizing the straight-line method over the estimated useful lives for owned assets, ranging from 5 to 7 years.

Impairment of Long-Lived Assets

The Company evaluates its long-lived assets for impairment, in accordance with the provisions established under Statement of SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets", when events or changes in circumstances indicate that the related carrying amount may not be recoverable. An impairment is considered to exist if the total estimated future cash flows on an undiscounted basis is less than the carrying amount of the related assets. An impairment loss is measured and recorded based on the discounted estimated future cash flows. Changes in significant assumptions underlying future cash flow estimates or fair values of assets may have a material effect on the Company's financial position and results of operations.

**TETON PETROLEUM COMPANY****Notes to Consolidated Financial Statements  
For The Years Ended December 31, 2004, 2003 and 2002****Note 1 - Description of Business and Summary of Significant Accounting Policies (continued)**Asset Retirement Obligations

During 2003 the Company applied the provisions of SFAS No. 143, "Accounting for Asset Retirement Obligations." The Company recorded \$126,500 as the fair value of the Company's estimated liability for the retirement of its Russian oil and gas assets along with a corresponding increase in the carrying value of the related oil and gas properties as of December 31, 2003, as the effect of adopting SFAS No. 143 on January 1, 2003 was not material. Had the Company adopted SFAS No. 143 on January 1, 2002 the net loss to common shareholders would have been increased by \$13,000.

Stock-Based Compensation

In December 2002, the FASB issued SFAS No. 148 "Accounting for Stock-Based Compensation- Transition and Disclosure." This statement amends SFAS No. 123, "Accounting for Stock-Based Compensation" to provide alternative methods of transition for an entity that voluntarily changes to the fair value method of accounting for stock-based compensation. In addition, SFAS 148 amends the disclosure provision of SFAS 123 to require more prominent disclosure about the effects of an entity's accounting policy decisions with respect to stock-based employee compensation on reported results of operations. The Company has adopted the disclosure-only provisions of Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation." Accordingly, no compensation cost has been recognized for stock options issued to employees, officers and directors under the stock option plan. Had compensation cost for the Company's options issued to employees, officers and directors been determined based on the fair value at the grant date for awards consistent with the provisions of SFAS No. 123, as amended by SFAS No. 148, the Company's net loss and basic loss per common share would have been changed to the pro forma amounts indicated below:

|   | 2004         | For the Years Ended December 31, |    | 2002         |
|---|--------------|----------------------------------|----|--------------|
|   |              | 2003                             |    |              |
| Net income (loss) applicable to common shareholders - as reported | \$ 7,190,301 | \$ (8,415,537)                   | \$ | (10,973,923) |
| Fair value of employee compensation expense                       | 3,512,305    | 4,974,141                        |    | 972,041      |
| Net income (loss) applicable to common shareholders - pro forma   | \$ 3,677,996 | \$ (13,389,678)                  | \$ | (11,945,964) |
| Basic income (loss) per common share - as reported                | \$ .73       | \$ (1.23)                        | \$ | (3.53)       |
| Basic income (loss) per common share - pro forma                  | \$ .41       | \$ (1.96)                        | \$ | (3.84)       |

**TETON PETROLEUM COMPANY****Notes to Consolidated Financial Statements  
For The Years Ended December 31, 2004, 2003 and 2002****Note 1 - Description of Business and Summary of Significant Accounting Policies (continued)**

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted-average assumptions used:

|   | For the Years Ended December 31, |              |      |
|---|----------------------------------|--------------|------|
|   | 2004                             | 2003         | 2002 |
| Approximate risk free rate                    | 4.06%                            | 4.00%        | --   |
| Average expected life                         | 10 years                         | 10 years     | --   |
| Dividend yield                                | -%                               | -%           | --   |
| Volatility                                    | 55.0%                            | 100%         | --   |
| Estimated fair value of total options granted | \$ 3,512,305                     | \$ 4,974,141 | --   |
| Estimated fair value per option granted       | \$ 2.48                          | \$ 3.15      | --   |

As described in Note 5, 994,000 options granted to the Board of Directors with an estimated fair value of \$2,465,120 under the Company's 2003 Stock Option Plan have been treated as issued and outstanding.

**Foreign Currency Translation**

All assets and liabilities of the Company's subsidiary were translated into U.S. dollars using the prevailing exchange rates as of the balance sheet date. Income and expenses are translated using the weighted average exchange rates for the period. Stockholders' investments are translated at the historical exchange rates prevailing at the time of such investments. Any gains or losses from foreign currency translation are included as a separate component of stockholders' equity. The prevailing exchange rates at June 30, 2004 and December 31, 2003 and 2002 were approximately 1 U.S. dollar to 29.03, 29.45 and 31.78, Russian rubles, respectively. For the six months ended June 30, 2004 and the years ended December 31, 2003 and 2002, the average exchange rate for 1 U.S. dollar was 28.76, 30.66 and 31.39, Russian rubles, respectively.

**Basic Loss Per Share**

The Company applies the provisions of Statement of Financial Accounting Standard No. 128, "Earnings Per Share" (FAS 128). All dilutive potential common shares have an antidilutive effect on diluted per share amounts and therefore have been excluded in determining net loss per share. The Company's basic and diluted loss per share are equivalent and accordingly only basic loss per share has been presented.

The following table reflects the effects of dilutive securities as of December 31:

|  | 2004       | 2003       | 2002      |
|--|------------|------------|-----------|
| Dilutive effects of options                      | 2,993,037  | 1,578,037  | --        |
| Dilutive effects of warrants                     | 7,359,728  | 7,389,981  | 4,587,780 |
| Dilutive effects of convertible preferred shares | 281,460    | 2,381,351  | --        |
|  | 10,634,224 | 11,349,369 | 4,587,780 |



**TETON PETROLEUM COMPANY**

**Notes to Consolidated Financial Statements  
For The Years Ended December 31, 2004, 2003 and 2002**

**Note 1 - Description of Business and Summary of Significant Accounting Policies (continued)**

Such securities have been excluded from the earnings per share calculation as their effect was anti-dilutive. However, such securities could dilute future earnings, if achieved. The 2002 and 2003 share and per share amounts have been adjusted to reflect the 1 for 12 reverse split approved by the shareholders on March 19, 2003.

**Fair Value of Financial Instruments**

The carrying amounts of financial instruments including cash, accounts payable and accrued liabilities approximated fair value as of December 31, 2004 and 2003 because of the relatively short maturity of these instruments.

The Company is exposed to foreign currency risks to the extent that transactions and balances are denominated in currencies other than the United States dollar.

**Income Taxes**

The Company recognizes deferred tax liabilities and assets based on the differences between the tax basis of assets and liabilities and their reported amounts in the financial statements that will result in taxable or deductible amounts in future years. The measurement of deferred tax assets may be reduced by a valuation allowance based upon management's assessment of available evidence if it is deemed more likely than not some or all of the deferred tax assets will not be realizable.

F - 15

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**TETON PETROLEUM COMPANY**

**Notes to Consolidated Financial Statements  
For The Years Ended December 31, 2004, 2003 and 2002**

**Note 1 - Description of Business and Summary of Significant Accounting Policies (continued)**

Reclassifications

Certain amounts in the 2002 and 2003 consolidated financial statements have been reclassified to conform to the 2004 presentation.

Recently Issued Accounting Pronouncements

In December 2004, the Financial Accounting Standards Board ("FASB") issued SFAS No. 123 (revised 2004), "Share-Based Payment." SFAS No. 123R replaced SFAS No. 123 and superseded APB 25. SFAS No. 123R will require compensation cost related to share-based payment transactions to be recognized in financial statements. As permitted by SFAS No. 123, the Company elected to follow the guidance of APB 25, which allowed companies to use the intrinsic value method of accounting to value their share-based payment transactions with employees. Based on this method, the Company did not recognize compensation expense in its financial statements as the stock options granted had an exercise price equal to the fair market value of the underlying Common Stock on the date of the grant. SFAS No. 123R requires measurement of the cost of share-based payment transactions to employees at the fair value of the award on the grant date and recognition of expense over the requisite service or vesting period. SFAS No. 123R requires implementation using a modified version of prospective application, under which compensation expense for the unvested portion of previously granted awards and all new awards will be recognized on or after the date of adoption. SFAS No. 123R also allows companies to adopt SFAS No. 123R by restating previously issued financial statements, basing the amounts on the expense previously calculated and reported in their pro forma footnote disclosures required under SFAS No. 123. The Company has not decided which adoption method will be used. The provisions of SFAS No. 123R will be adopted by the Company effective July 1, 2005. The effect of the adoption of SFAS No. 123R is expected to be comparable to that disclosed on a pro forma basis as a result of applying the current fair value recognition provisions of SFAS No. 123.

In December 2004, the FASB issued SFAS No. 153 "Exchanges of Non-monetary Assets—an amendment of APB Opinion No. 29." This Statement amended APB Opinion No. 29 to eliminate the exception for non-monetary exchanges of similar productive assets and replaces it with a general exception for exchanges of non-monetary assets that do not have commercial substance. A non-monetary exchange has commercial substance if the future cash flows of the entity are expected to change significantly as a result of the exchange. The Company is currently evaluating the impact of this new standard, but believes that it will not have a material impact upon the Company's financial position, results of operations or cash flows.

**TETON PETROLEUM COMPANY****Notes to Consolidated Financial Statements  
For The Years Ended December 31, 2004, 2003 and 2002****Note 2 - Sale of Goloil**

As described in Note 1, the Company considers the sale of Goloil to be effective July 1, 2004. Accordingly, the operating activities of Goloil for the six months ended June 30, 2004 and the years ended December 31, 2003 and 2002 have been included in the results from discontinued operations, summarized as follows:

|  | 2004          | 2003           | 2002         |
|--|---------------|----------------|--------------|
| Sales  | \$ 6,552,138  | \$ 11,437,802  | \$ 6,923,320 |
| Cost of sales and expenses                                     | 7,072,272     | 12,604,234     | 7,319,997    |
| Loss from operations   | (520,134)     | (1,166,432)    | (396,677)    |
| Other income (expense)   |               |                |              |
| Interest expense   | (166,216)     | (347,740)      | (385,939)    |
| Net loss from discontinued operations, before tax              | (686,350)     | (1,514,172)    | (782,616)    |
| Income tax   | (16,829)      | (84,508)       | --           |
| Net loss from discontinued operations, before gain on disposal | (703,179)     | (1,598,680)    | (782,616)    |
| Gain on sale of ZAO Goloil stock                               | 13,086,761    | --             | --           |
| Income (loss) from discontinued operations                     | \$ 12,383,582 | \$ (1,598,680) | \$ (782,616) |

The gain on sale of Goloil stock is calculated as follows:

|   |    |            |
|---|----|------------|
| Sale price for Goloil shares                        | \$ | 8,960,229  |
| Less direct transaction expenses:                   |    |            |
| Investment banking fee                              |    | (750,000)  |
| Net fees and expenses                               |    | (246,779)  |
| Net proceeds  |    | 7,963,450  |
| Net deficit of investment in Goloil at date of sale |    | 5,123,311  |
| Gain on disposal of ZAO Goloil                      | \$ | 13,086,761 |

**TETON PETROLEUM COMPANY**

**Notes to Consolidated Financial Statements  
For The Years Ended December 31, 2004, 2003 and 2002**

**Note 3 - Notes Payable**

During 2003:

The Company received proceeds of \$628,750 from the issuance of promissory notes to three shareholders. In connection with these notes, 128,700 warrants valued at \$110,170 were issued. At December 31, 2003, the full amount of the discount had been amortized and recorded as a non-cash financing charge. The Company has recorded the value of these warrants using the Black-Scholes option-pricing model using the following assumptions: volatility of 73%, a risk-free rate of 3.5%, zero dividend payments, and a life of one year.

The Company paid \$478,750 of the promissory notes issued during the year. The remaining \$150,000 along with accrued interest of \$9,426 were exchanged for Teton's 8% convertible preferred shares.

During 2002:

The scheduled March 1, 2002 principal payments on two notes payable totaling \$250,000 to stockholders were extended to April 15, 2002. In exchange for this extension, the holders were issued 10,417 stock purchase warrants, with an exercise price of \$6.00 that expired February 2004, which had been valued at \$14,469 using the Black Scholes option pricing model with assumptions of volatility of 100%, risk free rate of 5.5% and no dividend yield. These extensions were recorded in the first quarter of 2002 as financing costs. These notes were fully paid off in 2002.

The Company issued 143,678 warrants in connection with related party notes payable of \$450,000 and \$50,000. The warrants were valued at \$156,781 and recorded as financing costs. Additionally, in the first quarter of 2002, the due dates of the two notes payable totaling \$500,000 were extended by the holders to April 15, 2002. As consideration for this extension the Company agreed to modify the expiration dates of certain warrants previously held by the note holders from October 31, 2002 to January 31, 2003. These extensions were valued based upon the incremental fair value of the warrants on the date of modification, which totaled approximately \$32,000. The values were calculated using the Black Scholes option-pricing model under the assumptions described in the previous paragraph, and were recorded in the first quarter of 2002, the quarter the modifications occurred.

During 2002, the Company paid \$200,000 of a \$450,000 note payable outstanding at December 31, 2001. The remaining \$250,000 was converted into a convertible debenture with 83,333 warrants also being issued in connection with the Company's private placement offering of convertible debentures.

The Company also paid off a \$50,000 note payable to a stockholder and the \$94,210 note payable to an officer during 2002, which were outstanding at December 31, 2001.

During 2002, the Company received proceeds of \$300,000 on a note payable from a stockholder. In connection with the note, 41,667 warrants valued at \$150,016 were issued and recorded as financing charges. The Company paid off this note in November 2002. The Company has recorded the value of these warrants using the Black Scholes option-pricing model using the following assumptions: volatility of 138%, a risk-free rate of 4.5%, zero dividend payments, and a life of 2 years.

F - 18

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**TETON PETROLEUM COMPANY**

**Notes to Consolidated Financial Statements  
For The Years Ended December 31, 2004, 2003 and 2002**

**Note 4 - Stockholders' Equity**

Total expense recorded associated with the above warrant issuances and modifications totaled \$353,379 and have been recorded as non-cash financing charges during the year ended December 31, 2002.

**Changes in Stockholders' Equity during 2004**

**Private Placements of Common Stock**

During the year ended December 31, 2004, 45,925 common shares were issued for (i) the settlement of accrued liabilities of \$58,700; and (ii) services provided by consultants of \$43,329 and (iii) services provided by the advisory board of \$58,000.

50,000 warrants were issued to settle a liability at December 31, 2003 valued at \$46,967. We also issued 100,000 warrants to a consultant valued at \$102,094 for services.

**Private Placements of Series A Convertible Preferred Stock**

The Company received the following proceeds from the issuance of privately placed preferred stock at a price of \$4.35 per share:

Proceeds of \$499,998 (net of cash costs of \$50,000) from the issuance of 126,436 shares of 8% convertible preferred stock.

The preferred stock carries an 8% dividend, payable quarterly commencing January 1, 2004 and is convertible into common stock at a price of \$4.35 per share. The preferred stock is entitled to vote on all matters presented to the Company's common stockholders, with the number of votes being equal to the number of underlying common shares. The preferred stock also contains a liquidation preference of \$4.35 per share plus accrued unpaid dividends. The preferred stock can be redeemed by the Company after one year for \$4.35 per share upon proper notice of redemption being provided by the Company.

**Changes in Stockholders' Equity during 2003**

On March 19, 2003, the stockholders authorized an increase in the Company's common shares from 100,000,000 to 250,000,000 and authorized 25,000,000 shares of preferred stock for future issuance. In addition, the stockholders approved a 1 to 12 reverse stock split.

**Private Placements of Common Stock**

During the year ended December 31, 2003 the Company received the following proceeds from the issuance of privately placed common stock:

\$1,091,900 (net of costs of \$98,100) from the issuance of 437,012 shares of common stock. In connection with the private placement, the Company also issued a warrant for each \$3.00 stock investment. The warrants have a term of two years and an exercise price of \$6.00,



**TETON PETROLEUM COMPANY**

**Notes to Consolidated Financial Statements  
For The Years Ended December 31, 2004, 2003 and 2002**

**Note 4 - Stockholders' Equity (continued)**

\$1,939,610 during the year ended December 31, 2003 related to outstanding stock subscriptions receivable at December 31, 2002,

80,828 common shares valued at \$317,902 were issued for (i) settlement of accounts payable and accrued liabilities of \$220,000; and (ii) services provided by the advisory board of \$97,902.

**Private Placements of Series A Convertible Preferred Stock**

During the year ended December 31, 2003 the Company received the following proceeds from the issuance of privately placed preferred stock issued at an offering price of \$4.35 per share.

Proceeds of \$9,145,450 (net of cash costs of \$473,888 and net of \$46,968 related to the obligation to issue warrants for capital raising) from the issuance of 2,266,680 shares of 8% convertible preferred stock.

\$14,574 from the issuance of 40,000 preferred shares in exchange for a \$150,000 note payable outstanding and accrued interest of \$9,426.

We also issued 12,000 preferred shares to a consultant for capital raising services valued at \$52,200.

The preferred shares carry an 8% dividend, payable quarterly commencing January 1, 2004 and are convertible into common stock at a price of \$4.35 per share. The preferred stock is entitled to vote on all matters presented to the Company's common stockholders, with the number of votes being equal to the number of underlying common shares. The preferred stock also contains a liquidation preference of \$4.35 per share plus accrued unpaid dividends. The preferred shares can be redeemed by the Company after one year for \$4.35 per share, under certain circumstances and upon proper notice of redemption being provided by the Company.

In connection with the preferred share private placement for Tranches 1 and 2, certain placements were entered into when the underlying price of the common stock to which the preferred shares are convertible into, exceeded \$4.35, the stated conversion rate. As a result of the underlying shares being in-the-money, the Company was required to compute a beneficial conversion charge, which is calculated as the difference between the conversion price of \$4.35 and the closing stock price on the effective date of each offering, multiplied by the total of the related common shares to be issued upon conversion of the preferred stock. These charges are reflected as a dividend to the preferred shareholders and are recognized over the period in which the preferred stock first becomes convertible. For the Tranche 1 shares the charge was immediately recognized as the shares were immediately convertible into common. For Tranche 2 the shares could not be converted until a shareholder vote on January 27, 2004 took place approving the issuance of additional common shares. The calculated beneficial conversion feature on Tranche 2 was therefore amortized from the effective date of each issuance through January 27, 2004. This resulted in total beneficial conversion charges of \$ 1,182,452, of which \$1,063,842 were recorded during the fourth quarter of 2003, and \$118,610 will be amortized and recorded as preferred dividends in January of 2004.

**TETON PETROLEUM COMPANY**

**Notes to Consolidated Financial Statements  
For The Years Ended December 31, 2004, 2003 and 2002**

**Note 4 - Stockholders' Equity (continued)**

The Company also sent each preferred shareholder an inducement offer to convert their shares of preferred into common shares. If converted within 60 days of closing, the investors were entitled to receive (i) dividends payable in common stock equivalent to one year's worth of dividends; and (ii) Class B Warrants to purchase two shares of common stock for each \$10 invested, exercisable at \$6.00 per share.

**Private Placements of Series A Convertible Preferred Stock (continued)**

In connection with the preferred share private placement for Tranche 1, shareholders converted 1,645,099 of 8% convertible preferred shares to common stock at a price of \$4.35 per share. Common share dividends of 8% for a full year were paid totaling \$546,173 and 1,431,237 warrants were issued valued at \$1,170,678, for a total inducement charge of \$1,716,851 recognized as a preferred dividend during the fourth quarter for those investors which accepted the inducement offer. The warrants issued were valued using the Black-Scholes option pricing model using the following assumptions: volatility of 55%, a risk-free rate of 1.875%, zero dividend payments, and a life of two years.

In connection with the preferred share private placement for Tranche 2, a common share dividend of 8% for a full year was paid totaling \$157,601 and warrants were issued valued at \$337,805, for a total inducement charge of \$495,406 which will be recognized as a preferred dividend in the first quarter of 2004, associated with the preferred stock inducement offer ending on March 27, 2004. The warrants issued were valued using the Black-Scholes option pricing model using the following assumptions: volatility of 55%, a risk-free rate of 1.875%, zero dividend payments, and a life of two years.

**Warrants to Purchase Common Shares**

During 2003, the Company issued 440,140 warrants to entities for their services directly related to raising capital under private placements. The Company also issued 128,700 warrants in conjunction with debt valued at \$110,170.

During 2003, the Company issued 1,019,883 warrants in connection with common stock private placement offerings, with an exercise price of \$6.00 that expire December 30, 2004.

**Changes in Stockholders' Equity during 2002**

*Private Placements of Common Stock*

During the year ended December 31, 2002 the Company received the following proceeds from the issuance of privately placed common stock:

\$3,333,460 from the issuance of 1,223,737 shares of common stock. In connection with the private placement offerings, the Company also issued a warrant for each \$3.00 stock investment. The warrants have a term of two years and an exercise price of \$6.00.

\$605,136 from the issuance of 221,198 common shares issued for consulting services.

**TETON PETROLEUM COMPANY**

**Notes to Consolidated Financial Statements  
For The Years Ended December 31, 2004, 2003 and 2002**

**Note 4 - Stockholders' Equity (continued)**

\$23,200 from the issuance of 7,407 common shares for services provided in 2001. The Company accrued a liability for this amount at December 31, 2002.

**Changes in Stockholder Equity During 2002 (continued)**

*Convertible Debentures*

During 2002, the Company received proceeds of \$4,163,143 from the private placement of convertible debentures. The debentures had a term of three years from April 1, 2002 and provided for interest at 10% per annum payable annually. The debentures provided that the holder may convert the debenture and accrued interest into shares of common stock at a \$3 conversion rate.

The debentures also included warrants to purchase common stock and have an exercise price of \$6 and a term of two years. Each debenture holder received one warrant for each \$.25 (pre-split) of investment made in debentures.

On September 1, 2002, the Company redeemed all debentures outstanding for shares of its common stock. The debentures were redeemed at 110% of their face value by issuing one share of common stock for each \$3 of redemption value, which also incorporates any accrued interest through September 1, 2002. Financing charges were recorded for the difference between the cumulative 10% contractual interest accrued through September 1, 2002 and the 10% premium paid upon redemption, which totaled \$466,771.

As a result of the warrants issued with the debentures and in-the-money conversion features present at issuance, non-cash financing charges of \$4,714,625 were expensed. While the stock to which the conversion rights and warrants apply is restricted stock, the valuation with respect to this stock in calculating the discount was "as if" the stock was immediately salable. The effect of this is to make the amount of discount and its related amortization higher than it would otherwise have been. Management believes these costs are non-recurring and will manage future capital raising programs to minimize or eliminate these costs.

*Warrants to Purchase Common Shares*

During 2002, the Company issued 133,333 warrants to consultants for services valued at \$215,086. The Company also issued 616,793 to employees and directors for services performed.



**TETON PETROLEUM COMPANY**

**Notes to Consolidated Financial Statements  
For The Years Ended December 31, 2004, 2003 and 2002**

**Note 4 - Stockholders' Equity (continued)**

Changes in Stockholder Equity during 2002 (continued)

*Warrants to Purchase Common Shares (continued)*

The following table presents the activity for warrants outstanding:

|                                 | Shares | Weighted<br>Average<br>Exercise<br>Price |
|---------------------------------|--------|--|
| Outstanding - December 31, 2001 |        | 544,098                                  |
| \$                              |        | 5.28                                     |
| Granted                         |        | 4,068,682                                |
|                                 |        | 5.52                                     |
| Forfeited/canceled              |        | (25,000                                  |
| )                               |        | 2.04                                     |
| Outstanding - December 31, 2002 |        | 4,587,780                                |
|                                 |        | 5.52                                     |
| Granted                         |        | 3,210,249                                |
|                                 |        | 2.49                                     |
| Forfeited/canceled              |        |  |

|                                 |             |
|---------------------------------|-------------|
| )                               | (408,048)   |
|                                 | 0.30        |
| Outstanding - December 31, 2003 |             |
|                                 | 7,389,981   |
|                                 | 5.63        |
| Granted                         |             |
|                                 | 4,496,142   |
|                                 | 6.00        |
| Forfeited/canceled              |             |
| )                               | (4,526,396) |
|                                 | 5.98        |
| Outstanding - December 31, 2004 |             |
|                                 | 7,359,727   |
| \$                              |             |
|                                 | 5.62        |

On May 11, 2004 the Board of Directors voted to extend by one year the expiration date of certain warrants issued during the period from April 1, 2002 to December 15, 2003, with no change in the exercise price of \$6.00. The above table includes the extension as an expiration and grant of such warrants.

The following table presents the composition of warrants outstanding and exercisable:

| Range of Exercise Prices | 2004<br>Shares Outstanding<br>Number | Price*  | Life* |
|--------------------------|--------------------------------------|---------|-------|
| \$2.72 - \$3.48          | 903,271                              | \$ .36  | 0.79  |
| \$4.35 - \$6.00          | 6,414,788                            | 5.20    | 0.68  |
| \$9.00 - \$12.00         | 41,668                               | .06     | 0.01  |
| Total - December 31      | 7,359,727                            | \$ 5.62 | 1.48  |

\*Price and Life reflect the weighted average exercise price and weighted average remaining contractual life, respectively.

F - 23

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**TETON PETROLEUM COMPANY**

**Notes to Consolidated Financial Statements  
For The Years Ended December 31, 2004, 2003 and 2002**

**Note 5 - Stock Options**

At the annual meeting on March 19, 2003, the Company's shareholders approved an employee stock option plan and authorized 25,000,000 shares of Common Stock for issuance thereunder. At the same annual meeting at which the 2003 Plan was adopted, the Company's shareholders also approved a 1:12 reverse split. Although the Board of Directors believed that a reasonable interpretation of both actions indicated that since the 2003 Plan was adopted at the same shareholders meeting as the reverse split and further since there were no shares technically outstanding at the time of the reverse split's approval, that no adjustment need be made to the plan, it nevertheless elected to take a conservative approach and to remove any ambiguity by asking the stockholders, at the Company's 2005 annual meeting, to approve a total pool of 3,000,000 options available for grant under the 2003 plan.

Under the plan, incentive and non-qualified options may be granted. During the second quarter of 2003, the Company issued 30,000 non-qualified options to outside advisory board members which has been recorded as compensation expense during the three-months ended June 30, 2003 valued at \$94,701, using the Black-Scholes option-pricing model with the following assumptions: volatility of 100%, a risk-free rate of 4%, zero dividend payments, and a life of ten years. On April 9, 2003 the Company issued 1,448,037 incentive options to employees, officers and directors valued at \$4,571,026 using the Black-Scholes option-pricing model under the same assumptions described above. On August 3, 2003, 100,000 options valued at \$308,414 were issued to a director under the Company Plan. On March 30, 2004 1,415,000 options valued at \$3,512,305 using the same assumptions as above were issued to employees, officers and directors. The Board issued the options in 2004 with the understanding that they would seek clarification from shareholders as to the ultimate number of options that can be issued. Accordingly, 994,000 of the options representing approximately \$2,500,000 of the fair value of the total options granted could be voided if the shareholders do not approve an increase in the number of authorized shares available for issuance under the 2003 Employee Stock option plan.

As of December 31, 2004, 1,478,037 options with an exercise price of \$3.48, 100,000 options with an exercise price of \$3.71 and 1,415,000 options with an exercise price of \$3.60 were outstanding. The weighted average fair value and contractual life of these issues were \$2.48, \$3.26 and \$3.71 and 10.00, 8.59 and .61 years, respectively.

**TETON PETROLEUM COMPANY****Notes to Consolidated Financial Statements  
For The Years Ended December 31, 2004, 2003 and 2002****Note 5 - Stock Options (continued)**

The following table presents the activity for stock options outstanding and exercisable:

| Range of Exercise Prices        | Shares Outstanding |    | Price* | Life* |
|---------------------------------|--------------------|----|--------|-------|
|                                 | Number             |    |        |       |
| Outstanding - December 31, 2002 | -                  | \$ | -      | -     |
| Issued                          | 1,578,037          |    | 3.49   | 8.30  |
| Outstanding - December 31, 2003 | 1,578,037          | \$ | 3.49   | 8.30  |
| Issued                          | 1,415,000          |    | 3.60   | 9.25  |
| Outstanding - December 31, 2004 | 2,993,037          | \$ | 3.54   | 8.70  |

\*Price and Life reflect the weighted average exercise price and weighted average remaining contractual life, respectively.

**Note 6 - Income and Other Taxes**

The provision for income taxes from continuing operations consists of the following components:

|                  | 2004 | 2003 | 2002 |
|------------------|------|------|------|
| <b>Current:</b>  |      |      |      |
| Federal          | --   | --   | --   |
| State            | --   | --   | --   |
| Total current    | --   | --   | --   |
| <b>Deferred:</b> |      |      |      |
| Federal          | --   | --   | --   |
| State            | --   | --   | --   |
| Total Deferred   | --   | --   | --   |

Total income tax expense from continuing operations differed from the amounts computed by applying the federal statutory income tax rate of 35% to earnings (loss) before income taxes as a result of the following items for the years ended December 31:

|  | 2004           | 2003           | 2002           |
|--|----------------|----------------|----------------|
| Federal statutory income tax benefit from continuing operations                        | \$ (1,817,648) | \$ (1,412,657) | \$ (3,566,957) |
| State income tax benefit, net of federal income tax benefit from continuing operations | (154,367)      | (116,088)      | (326,347)      |
| Change in valuation allowance  | 1,955,312      | 1,470,453      | 4,133,733      |
| Other  | 16,703         | 58,292         | (240,429)      |
| Income tax expense   | --             | --             | --             |



**TETON PETROLEUM COMPANY****Notes to Consolidated Financial Statements  
For The Years Ended December 31, 2004, 2003 and 2002****Note 6 - Income and Other Taxes (continued)**

The tax effects of temporary differences that give rise to significant components of the Company's deferred tax assets and liabilities at December 31, 2004 and 2003 are as follows:

|  | 2004        | 2003        |
|--|-------------|-------------|
| Current Deferred Tax Assets (Liabilities)      |             |             |
| Other receivables                              | \$ (7,441)  | \$ (4,574)  |
| Prepaid expenses                               | (30,908)    | (36,363)    |
| A/P and accrued liabilities                    | 156,463     | 143,043     |
| Charitable contributions                       | --          | 4,088       |
| Valuation allowance                            | (118,114)   | (106,194)   |
| Net current deferred tax asset (liability)     | --          | --          |
| Non-Current Deferred Tax Assets (Liabilities)  |             |             |
| Depreciation                                   | (3,623)     | (3,462)     |
| Net Operating Loss                             | 4,478,522   | 7,107,951   |
| Valuation allowance                            | (4,474,899) | (7,104,489) |
| Net non-current deferred tax asset (liability) | --          | --          |
| Net Deferred Tax Asset (Liability)             | \$ --       | \$ --       |

At December 31, 2004, the Company had net operating loss carryforwards, for federal income tax purposes, of approximately \$11.8 million. These net operating loss carryforwards, if not utilized to reduce taxable income in future periods, will expire in various amounts beginning in 2018 through 2023. Such net operating loss is subject to U.S. Internal Revenue Code Section 382 limitations. Utilization of the NOL is limited to approximately \$900,000 per annum.

The Company has established a valuation allowance for deferred taxes that reduces its net deferred tax assets as management currently believes that these losses will not be utilized in the near term. The allowance recorded was \$4.6 million and \$7.2 million for 2004 and 2003 respectively. The Company reduced the valuation allowance in 2004 by approximately \$2.6 million due to the utilization of net operating loss carryforwards.

**Note 7 - Commitments**

Mr. Howard Cooper, Director, signed an employment contract on January 1, 2004 and then, upon his resignation as Executive Chairman, signed a consulting agreement with the Company dated March 1, 2005 to replace the employment contract. The consulting agreement is for a one year term, whereby Mr. Cooper will receive bi-monthly base payments of \$8,333 each. Under the terms of the agreement, if Mr. Cooper is terminated other than for cause, Mr. Cooper is entitled to 12 months of severance pay, payable in bi-monthly installments over 12 months, from the date of termination. The Company may discontinue the severance payments if Mr. Cooper violates the confidentiality, noncompetition, or nonsolicitation provisions of his employment agreement.

**TETON PETROLEUM COMPANY**

**Notes to Consolidated Financial Statements  
For The Years Ended December 31, 2004, 2003 and 2002**

**Note 7 - Commitments (continued)**

Mr. Arleth, President and Chief Executive Officer, signed an employment agreement on May 1, 2003. The agreement is for a three-year term, with an initial salary of \$10,000 per month that was increased to \$15,000 per month beginning in January 2004. Under the terms of the agreement, Mr. Arleth is entitled to 24 months severance pay in the event of a change of position or control of the Company.

**Note 8 - Subsequent Events**

On January 5, 2005 the Company entered into a definitive purchase and sale agreement for the acquisition of certain oil and gas leases covering up to 180,000 acres in North America. The closing of the transaction is subject to the satisfactory results of a due diligence investigation and delivery by the sellers of at least 138,063 acres with acceptable title and environmental conditions. The transaction is currently pending and the terms are being kept confidential subject to a request for confidential treatment previously filed with the Securities and Exchange Commission. The Company paid a nonrefundable deposit of \$25,000 in December upon signing a letter of intent. Earnest money of \$322,000 was paid in January upon signing the purchase and sale agreement. The balance due in cash, stock and warrants will be paid at closing. The Company expects to close the transaction on or before April 15, 2005.

On February 15, 2005, the Company signed a membership interest purchase agreement with PGR Partners, LLC ("PGR") whereby the Company acquired 25% of the membership interest in Piceance Gas Resources, LLC, a Colorado limited liability company ("Piceance LLC"). Piceance LLC owns certain oil and gas rights and leasehold assets covering approximately 6,300 acres in the Piceance Basin in Western Colorado. The properties owned by Piceance LLC carry a net revenue interest of 78.75%.

The purchase price for the membership interest in Piceance LLC was \$5.25 million in cash, the issuance of 450,000 unregistered shares of our common stock, which had a fair market value on the date of closing of \$720,000, and the issuance of warrants to purchase 200,000 shares of our common stock, exercisable for a period of five years at an exercise price of \$2.00 per share. Pursuant to the terms of the operating agreement, the Company is obligated to fund its share of the construction of a road on the leased area and 8 wells to be drilled during 2005.

On February 22, 2005, Mr. Cooper resigned as Executive Chairman of the Company. Mr. Cooper will remain on the Company's Board and will stand for reelection at the Company's upcoming annual meeting in May. In addition, Mr. Cooper will remain a consultant to the Company. On February 22, 2005, our Board elected James J. Woodcock, an outside director, as non-executive chairman of the Company.



**TETON PETROLEUM COMPANY****Notes to Consolidated Financial Statements  
For The Years Ended December 31, 2004, 2003 and 2002****Note 9 - Supplemental Oil and Gas Disclosures**

The following is a summary of costs incurred in oil and gas producing activities:

The Company sold its oil and gas producing activities during 2004. See Notes 1 and 2 to the financial statements.

Included below is the Company's investment and activity in oil and gas producing activities prior to the sale, which includes a proportionate share of ZAO Goloil's oil and gas properties, revenues, and costs.

|                          | 2004         | For the Years Ended December 31, |              |
|--------------------------|--------------|----------------------------------|--------------|
|                          |              | 2003                             | 2002         |
| Construction in progress | \$ -         | \$ 1,700,696                     | \$ -         |
| Development costs        | 2,988,882    | 5,207,931                        | 4,150,742    |
| Total                    | \$ 2,988,882 | \$ 6,908,627                     | \$ 4,150,742 |

The following reflects the Company's capitalized costs associated with oil and gas producing activities:

|  | 2004 | For the Years Ended December 31, |              |
|--|------|----------------------------------|--------------|
|  |      | 2003                             | 2002         |
| Property acquisition costs   | \$ - | \$ 595,558                       | \$ 595,558   |
| Construction in progress   | -    | 1,700,696                        | -            |
| Development costs  | -    | 10,808,813                       | 4,830,421    |
|  | -    | 13,105,067                       | 5,425,979    |
| Accumulated depreciation, depletion, amortization and valuation allowances | -    | (2,064,585)                      | (529,671)    |
| Net capitalized costs  | \$ - | \$ 11,040,482                    | \$ 4,896,308 |

**TETON PETROLEUM COMPANY****Notes to Consolidated Financial Statements  
For The Years Ended December 31, 2004, 2003 and 2002****Note 9 - Supplemental Oil and Gas Disclosures (continued)****Results of Operations from Oil and Gas Producing Activities**

Results of operations from oil and gas producing activities (excluding general and administrative expense, and interest expense) are presented as follows:

|   | For the Years Ended December 31, |               |              |
|---|----------------------------------|---------------|--------------|
|   | 2004                             | 2003          | 2002         |
| Oil and gas sales   | \$ 6,552,138                     | \$ 11,437,802 | \$ 6,923,320 |
| Oil and gas production                                      | (1,331,273)                      | (2,020,447)   | (1,218,411)  |
| Transportation and marketing                                | --                               | (807,266)     | (611,956)    |
| Export duties   | --                               | (1,492,999)   | (910,936)    |
| Taxes other than income taxes                               | (4,286,025)                      | (5,864,920)   | (3,537,990)  |
| Depletion, depreciation and amortization                    | (747,481)                        | (1,534,914)   | (451,930)    |
| Results of operations from oil and gas producing activities | \$ 187,359                       | \$ (282,744)  | \$ 192,097   |

**Reserves (Unaudited)**

Proved oil and gas reserves are the estimated quantities of crude oil, natural gas, and natural gas liquids which geological and engineering data demonstrate with reasonable certainty to be recoverable in future years from known reservoirs under existing economic and operating conditions. Proved development oil and gas reserves are those reserves expected to be recovered through existing wells with existing equipment and operating methods. The reserve data is based on studies prepared by an independent engineer. All proved reserves of oil and gas are located in Russia.

|   | For the Years Ended December 31, |             |              |
|---|----------------------------------|-------------|--------------|
|   | 2004                             | 2003        | 2002         |
| Proved reserves (bbls), beginning of period           | 8,262,000                        | 13,264,000  | 40,174,000   |
| Production  | (348,000)                        | (632,000)   | (471,000)    |
| Extension of reservoir                                | -                                | -           | 2,000,000    |
| Sale of reserves in place                             | (7,914,000)                      |             |              |
| Revisions of previous estimates                       | -                                | (4,370,000) | (28,439,000) |
| Proved reserves (bbls), end of period                 | -                                | 8,262,000   | 13,264,000   |
| Proved developed reserves (bbls), beginning of period | 3,816,000                        | 4,567,000   | 5,493,000    |
| Proved developed reserves (bbls), end of period       | -                                | 3,816,000   | 4,567,000    |

**TETON PETROLEUM COMPANY****Notes to Consolidated Financial Statements  
For The Years Ended December 31, 2004, 2003 and 2002****Note 9 - Supplemental Oil and Gas Disclosures (continued)****Standardized Measure of Discounted Future Net Cash Flows (Unaudited)**

SFAS No. 69 prescribes guidelines for computing a standardized measure of future net cash flows and changes therein relating to estimated proved reserves. The Company has followed these guidelines, which are briefly discussed below.

Future cash inflows and future production and development costs are determined by applying year-end prices and costs to the estimated quantities of oil and gas to be produced. Estimated future income taxes are computed using current statutory income tax rates for those countries where production occurs. The resulting future net cash flows are reduced to present value amounts by applying a 10% annual discount factor.

The assumptions used to compute the standardized measure are those prescribed by the Financial Accounting Standards Board and, as such, do not necessarily reflect the Company's expectations for actual revenues to be derived from those reserves nor their present worth. The limitations inherent in the reserve quantity estimation process, as discussed previously, are equally applicable to the standardized measure computations since these estimates are the basis for the valuation process.

The following summarizes the standardized measure and sets forth the Company's future net cash flows relating to proved oil and gas reserves based on the standardized measure prescribed in Statement of Financial Accounting Standards No. 69.

|   | For the Years Ended December 31, |                |                |
|---|----------------------------------|----------------|----------------|
|   | 2004                             | 2003           | 2002           |
| Future cash inflows                                       | \$ --                            | \$ 114,992,000 | \$ 230,581,000 |
| Future production costs                                   | --                               | (80,812,000)   | (151,167,000)  |
| Future development costs                                  | --                               | (14,595,000)   | (18,556,000)   |
| Future income tax expense                                 | --                               | (7,360,000)    | (16,365,000)   |
| Future net cash flows (undiscounted)                      | --                               | 12,225,000     | 44,493,000     |
| Annual discount of 10% for estimated timing of cash flows | --                               | (6,232,000)    | (19,069,000)   |
| Standardized measure of future net discounted cash flows  | \$ --                            | \$ 5,993,000   | \$ 25,424,000  |

**TETON PETROLEUM COMPANY****Notes to Consolidated Financial Statements  
For The Years Ended December 31, 2004, 2003 and 2002****Note 9 - Supplemental Oil and Gas Disclosures (continued)****Changes in Standardized Measure Base Case (Unaudited)**

The following are the principal sources of change in the standardized measure of discounted future net cash flows:

|   | For the Years Ended December 31, |               |               |
|---|----------------------------------|---------------|---------------|
|   | 2004                             | 2003          | 2002          |
| Standardized measure, beginning of period,  | \$ 5,993,000                     | \$ 25,424,000 | \$ 40,362,000 |
| Net changes in prices and production costs  | --                               | (11,038,000)  | 190,619,000   |
| Sales of oil and gas produced during period | (935,000)                        | (445,000)     | (644,000)     |
| Future development costs                    | --                               | (3,098,000)   | 22,344,000    |
| Revisions of previous quantity estimates    | --                               | (11,806,000)  | (274,605,000) |
| Extension of reservoir                      | --                               | --            | 19,867,000    |
| Accretion of discount                       | 299,950                          | 2,542,000     | 4,036,000     |
| Sale of reserves in place                   | (5,357,950)                      | --            | --            |
| Changes in income taxes, net                | --                               | 4,414,000     | 23,445,000    |
| Standardized measure, end of period         | \$ --                            | \$ 5,993,000  | \$ 25,424,000 |

**TETON PETROLEUM COMPANY****Notes to Consolidated Financial Statements  
For The Years Ended December 31, 2004, 2003 and 2002****Note 10 - Selected Quarterly Information (Unaudited)**

The following represents selected quarterly financial information for the years ended December 31, 2003 and 2004. Certain amounts have been reclassified to conform with the presentation in this Form 10-K.

| 2004   | For the Quarter Ended |                |              | December<br>31, |
|--|-----------------------|----------------|--------------|-----------------|
|  | March 31,             | June 30,       | Sept 30, (1) |                 |
| Loss from continuing operations  | \$ (2,086,915)        | \$ (1,712,408) | \$ (488,126) | \$ (905,832)    |
| Discontinued operations, net of tax  | (435,198)             | (267,981)      | 13,086,761   | --              |
| Net Income (Loss)  | (2,522,113)           | (1,980,389)    | 12,598,635   | (905,832)       |
| Basic and diluted loss per common share for continuing operations            | \$ (0.30)             | \$ (0.19)      | \$ (.07)     | \$ (.09)        |
| Basic and diluted income (loss) per common share for discontinued operations | \$ (.05)              | \$ (.03)       | \$ 1.45      | \$ .00          |
| Basic and diluted income (loss) per common share                             | \$ (.35)              | \$ (.22)       | \$ 1.38      | \$ (.10)        |
| 2003   |                       |                |              |                 |
| Loss from continuing operations  | \$ (773,774)          | \$ (981,898)   | \$ (984,080) | \$ (1,296,412)  |
| Discontinued operations, net of tax  | (7,311)               | (465,342)      | (768,087)    | (357,940)       |
| Net Income (Loss)  | (781,085)             | (1,447,240)    | (1,752,167)  | (1,654,352)     |
| Basic and diluted loss per common share for continuing operations            | \$ (0.12)             | \$ (0.15)      | \$ (.15)     | \$ (.58)        |
| Basic and diluted income (loss) per common share for discontinued operations | \$ (.00)              | \$ (.07)       | \$ (.11)     | \$ (.05)        |
| Basic and diluted income (loss) per common share                             | \$ (.12)              | \$ (.22)       | \$ (0.26)    | \$ (.63)        |

(1) The gain from the sale of Goloil stock included in results from discontinued operations for the quarter ended September 30, 2004 has been adjusted by approximately \$718,000 due to an error in recording the foreign currency translation account at the time of the sale, partially offset by an over accrual of current income taxes due.

**TETON PETROLEUM COMPANY**

**Item 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE.**

None.

**ITEM 9A. CONTROLS AND PROCEDURES**

As of December 31, 2004, an evaluation was performed by our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures. Based on that evaluation, Our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were not completely effective during the year ended December 31, 2004. During 2003 the Company hired a U.S. Controller that was a Certified Public Accountant. During 2004 the Company hired a contract Chief Financial Officer who is also a CPA and has significant oil and gas accounting expertise. During the first quarter, the Company was in the process of selling its only operating assets. The CFO was responsible for assisting in the analysis of the sale and the consolidation of the Russian subsidiary for the first quarter. While the Form 10Q was being prepared, the CFO was also working with the legal team on the extensive proxy that was required for approval of such sale. The U.S. Controller was assigned responsibility for preparing the accounting entries and disclosures relating to equity transactions which occurred during the first quarter of 2004 and the second quarter of 2004, respectively. The controller consulted with its auditors who provided general guidance on the accounting standards which should be reviewed to ensure proper accounting and disclosure for these transactions. The Controller's work was not reviewed by the CFO. During the review of the first and second quarter form 10Qs it was noted by the Company's auditors that the Controller did not have adequate expertise to determine the proper accounting entries and disclosures related to accounting for preferred stock dividends, the issuance of stock options and the extension of warrants. The auditors proposed adjusting entries and noted disclosure deficiencies in Forms 10-Q for March 31, 2004 and June 30, 2004. These deficiencies by definition, were deemed to be a weakness in internal control. The Controller resigned after the first quarter and it is now Company policy that the CFO will prepare and or review all information included in the financial reports of the Company. In addition, the CFO will obtain additional training as needed. In our opinion, these measures are sufficient to address our internal control weakness.

In connection with the audit of the year ended December 31, 2004, there were no "changes" except that the Company's auditors reported to the Company's Audit Committee that the auditors' considered one matter involving the internal controls over financial reporting to be a material weakness, which concerned accounting for complex equity transactions.

**ITEM 9B. OTHER INFORMATION**

None.

**TETON PETROLEUM COMPANY****PART III****Item 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT****DIRECTORS AND EXECUTIVE OFFICERS**

Directors, executive officers, and significant employees of Teton, their respective ages and positions with Teton are as follows:

| Name                | Age | Position                    |
|---------------------|-----|-----------------------------|
| James J. Woodcock   | 66  | Chairman & Director         |
| Karl F. Arleth      | 56  | President and CEO, Director |
| John T. Connor, Jr. | 63  | Director                    |
| Thomas F. Conroy    | 66  | Director                    |
| H. Howard Cooper    | 48  | Director                    |
| Patrick A. Quinn    | 51  | Chief Financial Officer     |

JAMES J. WOODCOCK has been a director since 2002 and Chairman of the Company's Compensation Committee, since 2003 and Chairman of the Company since February 2005. Since 1981, Mr. Woodcock has been the owner and CEO of Hy-Bon Engineering Company, based in Midland, Texas. Hy-Bon is an engineering firm and manufacturer of vapor recovery, gas boosters, and casing pressure reduction systems for the oil industry. From 1997 to 2002, Mr. Woodcock was the chairman of Transrepublic Resources, a private oil and gas exploration firm located in Midland Texas. Since 1996, Mr. Woodcock has been a board member of Renovar Energy, a private waste to energy firm located in Midland Texas and was its Chairman of the Board until 2003.

KARL F. ARLETH, has been our president and CEO since May 2003 and a director since 2002. From 2002 to 2003, Mr. Arleth was the Chief Operating Officer and a Board Member of Sefton Resources, an oil and gas exploration and production company. Between 1999 and 2001 he served as Chairman and CEO of Eurogas Inc. in London. Ending in 1999, Mr. Arleth spent 21 years with Amoco and BP-Amoco. In 1998 he chaired the Board of the Azerbaijan International Operating Company (AIOC) for BP-Amoco in Baku, Azerbaijan. Concurrently in 1997-98, he was also President of Amoco Caspian Sea Petroleum Ltd. in Azerbaijan. In 1997, he served as Director of Strategic Planning for Amoco Corporations Worldwide Exploration and Production Sector in Chicago. From 1992 to 1996 Mr. Arleth was President of Amoco Poland Ltd. in Warsaw, Poland. Between 1977 and 1992, Mr. Arleth held positions with Amoco as an exploration and development geologist, project supervisor, manager and executive in the Exploration and Production sector in Denver, Tulsa, Chicago and Houston. In North America, he has significant exploration and production experience in the Rocky Mountains, mid-continent, the western U.S. and Alaska.

**TETON PETROLEUM COMPANY**

JOHN T. CONNOR, Jr. became a director in 2003 and chairs the Board's audit committee. He is the Founder and Portfolio Manager of the Third Millennium Russia Fund, a US based mutual fund specializing in the equities of Russian public companies. A former attorney at Cravath, Swaine & Moore in New York City, he has been a partner in leading law firms in New York, Washington and New Jersey. Mr. Connor is a member of the Council on Foreign Relations.

THOMAS F. CONROY, has been a director since 2002. Mr. Conroy is a Certified Public Accountant with an MBA from the University of Chicago. Since August 2004, Mr. Conroy has been the Chairman of Mann-Conroy-Eisenberg & Assoc. LLC, a life insurance and reinsurance consulting firm. Since 2001, Mr. Conroy has been a managing principal of Strategic Reinsurance Consultants International LLC, a life reinsurance consulting and brokerage firm. Ending in 2001, Mr. Conroy, spent 27 years with ING and its predecessor organizations, serving in various financial positions and leading two of its strategic business units as President. As President of ING Reinsurance, he established their international presence, setting up facilities in The Netherlands, Bermuda, Ireland and Japan. He also served as an Officer and Board Member of Security Life of Denver Insurance Company and its subsidiaries. Mr. Conroy briefly served as our interim CFO and secretary from April 2002 until April 2003.

H. HOWARD COOPER, H. Howard Cooper was our chairman from 1996 until February 2005. Mr. Cooper was our president and CEO from 1996 until May 2003. Mr. Cooper founded American Tyumen in November 1996. He served as a director and president of American Tyumen until the merger with the Company. In 1994, he was a principal with Central Asian Petroleum, an oil and gas company with its primary operations in Kazakhstan, located in Denver, Colorado. From 1992 to 1994 Mr. Cooper served with AIG, an insurance group in New York. Prior to founding Teton, Mr. Cooper was an independent landman, from 1981 - 1991, who developed oil and gas opportunities in the U.S. Rocky Mountain Region.

PATRICK A. QUINN, CPA, CVA. Mr. Quinn joined Teton in February 2004 to serve as the Company's Chief Financial Officer on a contract basis. For the past fifteen years Mr. Quinn has been the CEO of Quinn & Associates, P.C.. Mr. Quinn provides accounting, tax and auditing services primarily to the oil and gas industry. As a result, Mr. Quinn has extensive experience in U.S. oil and gas operations, including the Rocky Mountain, Mid-continent and Gulf Coast regions. He has provided accounting and tax services to Teton since its inception. In addition, Mr. Quinn has extensive experience in international oil and gas operations including serving as the Controller of Hamilton Oil Corporation from 1978 through 1986, which was the first company to produce oil in the U.K. sector of the North Sea.



**TETON PETROLEUM COMPANY**

All directors serve as directors for a term of one year or until his successor is elected and qualified. All officers hold office until the first meeting of the board of directors after the annual meeting of stockholders next following his election or until his successor is elected and qualified. A director or officer may also resign at any time.

**COMMITTEES OF THE BOARD OF DIRECTORS**

The Board of Directors has a Compensation Committee, an Audit Committee and a Governance and Nominating Committee. The Compensation Committee and Audit Committee currently consist of two directors John Connor, who is the Audit Committee financial expert, and James J. Woodcock. The Nominating Committee is made up of Mr. Woodcock and Mr. Conroy.

John Connor, James Woodcock and Tom Conroy are the board members determined to be independent under American Stock Exchange listing standards.

The purpose of the Compensation Committee is to review the Company's compensation of its executives, to make determinations relative thereto and to submit recommendations to the Board of Directors with respect thereto in order to ensure that such officers and directors receive adequate and fair compensation. The Compensation Committee met three times by teleconference during the last fiscal year.

The Audit Committee is responsible for the general oversight of audit, legal compliance and potential conflict of interest matters, including (a) recommending the engagement and termination of the independent public accountants to audit the financial statements of the Company, (b) overseeing the scope of the external audit services, (c) reviewing adjustments recommended by the independent public accountant and addressing disagreements between the independent public accountants and management, (d) reviewing the adequacy of internal controls and management's handling of identified material inadequacies and reportable conditions in the internal controls over financial reporting and compliance with laws and regulations, and (e) supervising the internal audit function, which may include approving the selection, compensation and termination of internal auditors.

For the fiscal year ended 2004, the Audit Committee conducted discussions with management and the independent auditor regarding the acceptability and the quality of the accounting principles used in the reports in accordance with Statements on Accounting Standards (SAS) No. 61. These discussions included the clarity of the disclosures made therein, the underlying estimates and assumptions used in the financial reporting and the reasonableness of the significant judgments and management decisions made in developing the financial statements. In addition, the Audit Committee discussed with the independent auditor the matters in the written disclosures required by Independence Standards Board Standard No. 1.

For the fiscal year ended 2004, the Audit Committee has also discussed with management and its independent auditors issues related to the overall scope and objectives of the audits conducted, the internal controls used by the Company, and the selection of the Company's independent auditor. Additional meetings were held with the independent auditor, with financial management present, to discuss the specific results of audit investigations and examinations and the auditor's judgments regarding any and all of the above issues.

The Audit Committee met four times by teleconference during 2004.

As provided in the Governance and Nominating Committee's charter and our Company's corporate governance principles, the Governance and Nominating Committee is responsible for identifying

**TETON PETROLEUM COMPANY**

individuals qualified to become Directors. The Governance and Nominating Committee seeks to identify director candidates based on input provided by a number of sources, including (a) the Governance and Nominating Committee members, (b) our other Directors, (c) our stockholders, (d) our Chief Executive Officer or Chairman, and (e) third parties such as professional search firms. In evaluating potential candidates for director, the Governance and Nominating Committee considers the entirety of each candidate's credentials.

**Code of Ethics**

The Company has adopted its Code of Ethics and Business Conduct that applies to all of the officers, directors and employees of the Company. The Code is posted on our website ([www.tetonpetroleum.com](http://www.tetonpetroleum.com)). We will disclose on our website any waivers of, or amendments to, our Code.

**Compliance with Section 16(b) of the Exchange Act**

Section 16(b) of the 1934 Act requires that the Company's Directors and certain of its officers file reports of ownership and changes of ownership of the Company stock with the SEC and AMEX. Based solely on copies of such reports provided to the Company, the Company believes that all Directors and officers filed on a timely basis all such reports required of them with respect to stock ownership and changes in ownership during 2004 except that Messrs. Arleth, Conroy, Connor, Cooper and Woodcock were late in reporting the grant of stock options under the 2003 Employee Stock Option Plan.

**TETON PETROLEUM COMPANY****Item 11. EXECUTIVE COMPENSATION.**

The following table sets forth information concerning the compensation received by Mr. Howard Cooper, the Chairman of Teton, and Mr. Karl Arleth who served as its president and chief executive officer during 2004 (Mr. Cooper and Mr. Arleth, the “named executive officers”):

**Summary Compensation Table**

| Name & Principal Position                          | Year | Annual Compensation |            |                                | Long Term Compensation |  |         |                        |
|--|------|---------------------|------------|--------------------------------|------------------------|--|---------|------------------------|
|  |      | Salary (\$)         | Bonus (\$) | Other Annual Compensation (\$) | Awards                 | Securities Underlying Options SARs (#) | Payouts | All Other Compensation |
| H. Howard Cooper, Chairman<br>CEO (until May 2003) | 2004 | 200,000             | 160,000*   | 8,200                          | 0                      | 400,000                                | 0       | 0                      |
|  | 2003 | 160,000             | 0          | 0                              | 0                      | 603,289                                | 0       | 0                      |
|  | 2002 | 160,000             | 50,000     | 0                              | 0                      | 375,000                                | 0       | 0                      |
| Karl F. Arleth<br>CEO                              | 2004 | 180,000             | 80,000*    | 16,800                         | 0                      | 300,000                                | 0       | 0                      |
|  | 2003 | 85,000              | 0          | 0                              | 0                      | 410,338                                | 0       | 0                      |

\*Bonus paid for 2003 performance.

**TETON PETROLEUM COMPANY****Stock Options****Options/SARs Grants During Last Fiscal Year**

The following table provides information related to options granted to our named executive officers during the fiscal year ended December 31, 2004.

| Name           | Number of Securities Underlying Options Granted | % of Total Options Granted in Fiscal 2004 (1) | Exercise Price Per Share | Expiration Date | Grant Date Present Value (2) |
|----------------|---|---|--------------------------|-----------------|------------------------------|
| Howard Cooper  | 400,000   | 28.3%   | \$ 3.60                  | 03/30/14        | \$ 992,000                   |
| Karl F. Arleth | 300,000   | 21.2%   | \$ 3.60                  | 03/30/14        | \$ 744,000                   |

(1) The exercise price of the stock options was based on the fair market value of the stock on the day of the grant.

(2) Valued using the Black-Scholes option pricing model using the following assumptions: volatility of 55%, a risk-free rate of 4.06%, zero dividend payments, and an expected life of ten years.

The Board issued the options in 2004 with the understanding that they would seek shareholder approval as to the ultimate number of options that can be issued. Accordingly, 994,000 of the options representing approximately \$2,500,000 of the fair value of the total options granted could be voided if the shareholders do not approve an increase in the number of authorized shares available for issuance under the 2003 Employee Stock option plan.

**Aggregated Option Exercises in Last Fiscal Year and Fiscal Year-End Option Value**

| Name           | Shares Acquired On Exercise | Value Realized | Number of Securities Underlying Unexercised Options | Value of Unexercised In-the-money Options |
|----------------|-----------------------------|----------------|---|---|
| Howard Cooper  |                             |                |   |   |
|                |                             |                |   | --  |
|                |                             |                |   | --  |
|                |                             |                |   | 1,003,289                                 |
|                |                             |                |   | --  |
| Karl F. Arleth |                             |                |   |   |

--  
--  
710,338  
--

**Employee Pension, Profit Sharing or Other Retirement Plans**

The Company does not have a defined benefit, pension plan, profit sharing, or other retirement plan.

**Compensation of Directors**

The Company pays its outside Directors an annual retainer of \$24,000, payable quarterly. In addition, at the Company's sole discretion, the Company may issue stock options or warrants to its directors. During 2004, the Company granted to its outside directors a total of 350,000 options, with an exercise price of \$3.60 and an expiration date of March 30, 2014.

**TETON PETROLEUM COMPANY**

**Employment Contracts**

Mr. Howard Cooper, Director, signed a consulting agreement with the Company dated March 1, 2005. The consulting agreement is for an initial term of one year and will continue for additional one year terms unless 60 days prior to the anniversary date either party gives notice of termination. Mr. Cooper will receive bi-monthly payments of \$8,333 each. Under the terms of the agreement, if Mr. Cooper is terminated without cause, he is entitled to 12 months of severance pay, payable in bi-monthly installments over 12 months, from the date of termination. The Company may discontinue the severance payments if Mr. Cooper violates the confidentiality, noncompetition, or nonsolicitation provisions of his employment agreement.

Mr. Arleth, President and Chief Executive Officer, signed an employment agreement on May 1, 2003. The agreement is for a three-year term, with an initial salary of \$10,000 per month that was increased to \$15,000 per month beginning in January 2004. Under the terms of the agreement, Mr. Arleth is entitled to 24 months severance pay in the event of a change of position or control of the Company.

**TETON PETROLEUM COMPANY****Item 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT.**

The following tables sets forth, as of March 10, 2005, the number of and percent of our common stock beneficially owned by (a) all directors and nominees, naming them, (b) the named executive officers, (c) our directors and executive officers as a group, without naming them, and (d) persons or groups known by us to own beneficially 5% or more of our common stock:

| Name and Address of Beneficial Owner  | Amount and Nature of Beneficial Ownership | Percent of Class    |
|---|---|---------------------|
| H. Howard Cooper<br>1600 Broadway, Suite 2400<br>Denver, Colorado 80202-4921    | 1,607,481 (1)                             | 14.35%              |
| Karl F. Arleth<br>1600 Broadway, Suite 2400<br>Denver, Colorado 80202-4921      | 908,412 (2)                               | 8.59%               |
| James J. Woodcock<br>2404 Commerce Drive<br>Midland, TX 79702                   | 774,684 (3)                               | 7.44%               |
| John T. Connor, Jr.<br>1600 Broadway, Suite 2400<br>Denver, Colorado 80202-4921 | 536,896 (4)                               | 5.32%               |
| Thomas F. Conroy<br>3825 S. Colorado Blvd.<br>Denver, CO 80110                  | 160,751 (5)                               | 1.63%               |
| All executive officers and Directors as a group (7 persons)                     |   | 3,988,224<br>30.26% |

%

(1) Includes (i) 145,857 shares of common stock, (ii) 458,335 shares underlying warrants, with exercise prices ranging from \$3.24 to \$12.00, (iii) 603,289 shares underlying options exercisable at \$3.48 per share and (iv) 400,000 shares underlying options exercisable at \$3.60 per share.

(2) Includes (i) 75,850 shares of common stock, (ii) 122,224 shares underlying warrants, with exercise prices ranging from \$3.24 to \$6.00 per share, (iii) 410,338 shares underlying options exercisable at \$3.48 per share and (iv) 300,000 shares underlying options exercisable at \$3.60 per share.

(3) Includes (i) 105,279 shares of common stock, (ii) 259,257 shares underlying warrants, with exercise prices ranging from \$3.24 to \$6.00 per share, (iii) 210,148 shares underlying options exercisable at \$3.48 per share and (iv) 200,000 shares underlying options exercisable at \$3.60 per share.





**TETON PETROLEUM COMPANY**

(4) Includes (i) 183,554 shares of common stock owned indirectly, (ii) 11,675 shares of common stock owned directly, (iii) 166,667 shares of common stock underlying warrants, exercisable at \$6.00 per share, which are owned indirectly, (iv) 100,000 shares of common stock underlying options exercisable at \$3.71 per share and (v) 75,000 shares of common stock underlying options exercisable at \$3.60 per share.

(5) Includes (i) 27,647 shares of common stock, (ii) 29,446 shares underlying warrants, with exercise prices ranging from \$3.24 to \$6.00, (iii) 28,658 shares underlying options exercisable at \$3.48 per share and (iv) 75,000 shares underlying options exercisable at \$3.60 per share.

**Item 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS.**Transactions Involving Mr. Howard Cooper

Mr. Cooper and Teton have entered into a consulting agreement. Mr. Cooper's consulting agreement with Teton is discussed at "EXECUTIVE COMPENSATION - Employment Contracts."

Transactions Involving Mr. Arleth

Mr. Arleth, President and Chief Executive Officer, signed an employment agreement on May 1, 2003. The agreement is for a three-year term, with an initial salary of \$10,000 per month that was increased to \$15,000 per month beginning in January 2004. Under the terms of the agreement, Mr. Arleth is entitled to 24 months severance pay in the event of a change of position or control of the Company.

**ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES.****Audit and Non-Audit Fees**

Aggregate fees for professional services rendered for the Company by Ehrhardt Keefe Steiner & Hottman P.C. as of or for the two fiscal years ended December 31, 2004 and 2003 are set forth below:

|                    | <b>Fiscal Year<br/>2004</b> | <b>Fiscal Year<br/>2003</b> |
|--------------------|-----------------------------|-----------------------------|
| Audit Fees         | \$ 74,053                   | \$ 141,917                  |
| Audit-Related Fees | 40,508                      | 51,047                      |
| Tax Fees           | 8,550                       | 6,500                       |
| Total              | \$ 123,111                  | \$ 199,464                  |

**TETON PETROLEUM COMPANY**

**Audit Fees** Aggregate fees for professional services rendered by Ehrhardt Keefe Steiner & Hottman PC in connection with its audit of our consolidated financial statements for the fiscal years 2004 and 2003 and the quarterly reviews of our financial statements included in Forms 10-Q.

**Audit-Related Fees** These were primarily related to SB-2 and SB-2/A filings for the registration of our stock, assistance with the AMEX application process, review of the proxy statement and Form 8-K, and reviews and discussions regarding accounting treatment of debt and equity transactions.

**Tax Fees** These were related to tax compliance and related tax services.

Ehrhardt Keefe Steiner & Hottman P.C. rendered no professional services to us in connection with the design and implementation of financial information systems in fiscal year 2004 or 2003.

**Policy on Audit Committee Pre-Approval of Audit and Permissible Non-Audit Services of Independent Auditors**

The Audit Committee pre-approves all audit and non-audit services provided by the independent auditors prior to the engagement of the independent auditors with respect to such services. The Chairman of the Audit Committee has been delegated the authority by the Committee to pre-approve interim services by the independent auditors other than the annual exam. The Chairman must report all such pre-approvals to the entire Audit Committee at the next committee meeting.

**TETON PETROLEUM COMPANY**

**ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES.**

**Exhibits.**

| Exhibit No. | Description   |
|-------------|---|
| 3.1.1       | Certificate of Incorporation of EQ Resources Ltd incorporated by reference to Exhibit 2.1.1 of Teton's Form 10-SB, filed July 3, 2001.                                |
| 3.1.2       | Certificate of Domestication of EQ Resources Ltd incorporated by reference to Exhibit 2.1.2 of Teton's Form 10-SB, filed July 3, 2001.                                |
| 3.1.3       | Articles of Merger of EQ Resources Ltd. and American-Tyumen Exploration Company incorporated by reference to Exhibit 2.1.3 of Teton's Form 10-SB, filed July 3, 2001. |
| 3.1.4       | Certificate of Amendment of Teton Petroleum Company incorporated by reference to Exhibit 2.1.4 of Teton's Form 10-SB, filed July 3, 2001.                             |
| 3.1.5       | Certificate of Amendment of Teton Petroleum Company incorporated by reference to Exhibit 2.1.5 of Teton's Form 10-SB, filed July 3, 2001.                             |
| 3.1.6       | Certificate of Designation for Series A Convertible Preferred Stock, incorporated by reference to Exhibit 3.1.6 of Teton's Form SB-2, filed January 27, 2004.         |
| 3.2         | Bylaws, as amended, of Teton Petroleum Company incorporated by reference to Exhibit 3.2 of our Form 10-QSB, filed August 20, 2002.                                    |
| 10.1        | Consulting Agreement dated March 1, 2005, between Teton Petroleum Company and H. Howard Cooper, filed herewith.   |
| 10.1.1      | Employment Agreement, dated May 1, 2002, between Teton Petroleum Company and H. Howard Cooper, filed herewith.  |
| 10.3        | Employment Agreement, dated May 1, 2003, between Teton Petroleum Company and Karl F. Arleth, filed herewith.  |
| 10.4        | 2003 Employee Stock Option Plan, filed herewith.  |
| 10.5        | 2004 Non-employee Stock Compensation Plan incorporated by reference to Appendix B to our Proxy Statement filed on June 14, 2004.                                      |
| 10.6        | Binding Letter of Intent dated December 17, 2004 filed herewith.  |
| 14.1        | Code of Ethics and Business Conduct, filed herewith   |
| 21.1        | List of Subsidiaries, filed herewith.   |
| 31.1        | Certification by Chief Executive Officer pursuant to Sarbanes -Oxley Section 302, filed herewith.   |

**TETON PETROLEUM COMPANY**

| Exhibit No. | Description   |
|-------------|---|
| 31.2        | Certification by Chief Financial Officer pursuant to Sarbanes -Oxley Section 302, filed herewith.               |
| 32.1        | Certification by Chief Executive Officer pursuant to 18 U.S. C. Section 1350, filed herewith.                   |
| 32.2        | Certification by Chief Financial Officer pursuant to 18 U.S. C. Section 1350, filed herewith.                   |
| 99. 1       | Audit Committee Charter incorporated by reference to Exhibit 99.4 of our Form 10-KSB/A filed on April 21, 2004. |

**TETON PETROLEUM COMPANY**

**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

**TETON PETROLEUM COMPANY**

By: /s/ Karl. F. Arleth

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Karl. F. Arleth, Chief Executive Officer  
Dated: May 6, 2005

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

| Signature   | Title  | Date        |
|---|--|-------------|
| <u>/s/ James J. Woodcock</u><br>James J. Woodcock | Chairman and Director                                    | May 6, 2005 |
| <u>/s/ Karl F. Arleth</u><br>Karl F. Arleth       | President and CEO<br>(principal executive officer)       | May 6, 2005 |
| <u>/s/ H. Howard Cooper</u><br>H. Howard Cooper   | Director   | May 6, 2005 |
| <u>/s/ Thomas F. Conroy</u><br>Thomas F. Conroy   | Director   | May 6, 2005 |
| <u>/s/ John Connor</u><br>John Connor             | Director   | May 6, 2005 |
| <u>/s/ Patrick A. Quinn</u><br>Patrick A. Quinn   | Chief Financial Officer<br>(principal financial officer) | May 6, 2005 |