

Edgar Filing: CROWN ENERGY CORP - Form 10-Q

CROWN ENERGY CORP
Form 10-Q
November 14, 2001

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2001

OR

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

For the transition period from _____ to _____

Commission file number 0-19365

CROWN ENERGY CORPORATION

(Exact name of registrant as specified in its charter)

Utah

87-0368981

(State or other jurisdiction of incorporation or organization)

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

215 South State Street, Suite 650, Salt Lake City, Utah, 84111

(Address of principal executive offices, zip code)

(801) 537-5610

(Registrant's telephone number, including area code)

Not applicable

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 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 No

Indicate the number of shares outstanding of each of the issuer's

Edgar Filing: CROWN ENERGY CORP - Form 10-Q

classes of common stock, as of the latest practicable date.

There were 13,635,581 shares of \$0.02 par value common stock outstanding as of November 12, 2001.

CROWN ENERGY CORPORATION

INDEX

	PAGE(S)
PART I. Financial Information	
ITEM 1. Financial Statements	
Condensed Consolidated Balance Sheets at September 30, 2001 (unaudited) and December 31, 2000	3
Condensed Consolidated Statement of Operations for the Three Months ended September 30, 2001 and 2000 (unaudited)	5
Condensed Consolidated Statement of Operations for the Nine Months ended September 30, 2001 and 2000 (unaudited)	6
Condensed Consolidated Statement of Cash Flows for the Nine Months ended September 30, 2001 and 2000 (unaudited)	7
Notes to Condensed Consolidated Financial Statements (unaudited)	9
ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations	13
ITEM 3. Quantitative and Qualitative Disclosures about Market Risk	16
PART II. Other Information	
ITEM 1. Legal Proceedings	17
ITEM 2. Changes in Securities	17
ITEM 3. Defaults upon Senior Securities	17
ITEM 4. Submission of Matters to a Vote of Security Holders	17
ITEM 5. Other Information	17
ITEM 6. Exhibits and Reports on Form 8-K	18
PART III. Signatures	19

Edgar Filing: CROWN ENERGY CORP - Form 10-Q

2

PART I - FINANCIAL INFORMATION

CROWN ENERGY CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS

ASSETS

ITEM 1. FINANCIAL STATEMENTS

	Sept. 30, 2001 [unaudited] -----	December 2000 -----
CURRENT ASSETS:		
Cash and cash equivalents	\$ 284,790	\$ 2,878,
Accounts receivable, net of allowance for uncollectible accounts of \$1,826,713 and \$1,827,896 at Sept. 30, 2001 and December 31, 2000, respectively	8,470,558	1,419,
Inventory	2,338,742	2,370,
Prepaid and other current assets	189,479	93,
	-----	-----
Total Current Assets	11,283,569	6,761,
PROPERTY PLANT, AND EQUIPMENT, Net	9,797,363	9,661,
OTHER INTANGIBLE ASSETS, Net	355,470	404,
OTHER ASSETS	227,503	225,
	-----	-----
TOTAL	\$21,663,905 =====	\$17,052, =====

The accompanying notes are an integral part of these consolidated financial statements.

3

CROWN ENERGY CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS

LIABILITIES AND STOCKHOLDERS' EQUITY

	Sept. 30, 2001 [unaudited] -----	December 2000 -----
CURRENT LIABILITIES		
Accounts payable	\$ 5,660,610	\$ 1,317,
Preferred stock dividends payable	1,100,000	800,
Accrued expenses	105,828	127,
Accrued interest	6,659,127	3,987,
Long-term debt - estimated current portion	338,183	273,
Line-of-credit to related party	14,935,222	14,935,

Edgar Filing: CROWN ENERGY CORP - Form 10-Q

Total current liabilities	28,798,970	21,440,
MINORITY INTEREST IN CONSOLIDATED JOINT VENTURES	475,116	427,
CAPITALIZATION:		
Long-term debt	11,243,039	11,336,
Redeemable preferred stock	4,938,680	4,896,
Common stockholders' equity	(23,791,900)	(21,049,
Total capitalization	(7,610,181)	(4,816,
TOTAL	\$21,663,905	\$17,052,

The accompanying notes are an integral part of these consolidated financial statements.

4

CROWN ENERGY CORPORATION
CONDENSED CONSOLIDATED STATEMENT OF OPERATIONS

	For the Three Septemb 2001 [unaudited]
SALES, Net of demerits	\$15,539,700
COST OF SALES	12,757,549
GROSS PROFIT	2,782,151
GENERAL AND ADMINISTRATIVE EXPENSES	926,719
INCOME (LOSS) FROM OPERATIONS	1,855,432
OTHER INCOME (EXPENSES):	
Interest income and other income	4,877
Interest expense	(652,960)
Interest expense from arbitration judgment	(1,164,574)
Equity in losses of unconsolidated equity affiliate	0
Total other expense, net	(1,812,657)
INCOME BEFORE INCOME TAXES	

Edgar Filing: CROWN ENERGY CORP - Form 10-Q

AND MINORITY INTERESTS	42,775

DEFERRED INCOME TAX BENEFIT	0
MINORITY INTEREST IN EARNINGS OF CONSOLIDATED JOINT VENTURE	2,930

NET INCOME	\$ 45,705

NET INCOME (LOSS) PER COMMON SHARE - Basic and diluted	\$ 0.00
	=====

The accompanying notes are an integral part of these consolidated financial statements.

5

CROWN ENERGY CORPORATION
CONDENSED CONSOLIDATED STATEMENT OF OPERATIONS

	For the Nine Months September 1, 2001 [unaudited]

SALES, Net of demerits	\$23,185,290
COST OF SALES	20,331,211

GROSS PROFIT	2,854,079
GENERAL AND ADMINISTRATIVE EXPENSES	2,518,780

INCOME (LOSS) FROM OPERATIONS	335,299

OTHER INCOME (EXPENSES):	
Interest income and other income	67,795
Gain on Insurance Settlement	278,492
Interest expense	(1,930,996)
Interest expense from arbitration judgment	(1,164,574)
Equity in losses of unconsolidated equity affiliate	0

Total other expense, net	(2,749,283)
LOSS BEFORE INCOME TAXES AND MINORITY INTERESTS	(2,413,984)

Edgar Filing: CROWN ENERGY CORP - Form 10-Q

DEFERRED INCOME TAX BENEFIT	0
MINORITY INTEREST IN EARNINGS OF CONSOLIDATED JOINT VENTURE	14,132 -----
NET LOSS	\$ (2,399,852) -----
NET LOSS PER COMMON SHARE - Basic and diluted	\$ (0.20) =====

The accompanying notes are an integral part of these consolidated financial statements.

6

CROWN ENERGY CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	For the Nine September 2001 [unaudited] -----
Cash Flows From Operating Activities:	
Net income (loss)	\$ (2,399,852) -----
Adjustments to reconcile net loss to net cash used by operating activities:	
Amortization, depreciation and depletion	563,586
Provision for doubtful accounts receivable	(1,183)
Stock issued for legal services	0
Equity in losses of unconsolidated affiliate	0
Minority interest	(14,132)
Change in assets and liabilities:	
Accounts receivable	(7,050,115)
Inventory	32,145
Other assets	(98,666)
Accounts payable	4,321,850
Accrued expenses	2,671,870 -----
Total adjustments	425,355 -----
Net Cash Used in Operating Activities	(1,974,497) -----
Cash Flows From Investing Activities:	
Investment in and advances to Crown Asphalt Ridge, LLC	0

Edgar Filing: CROWN ENERGY CORP - Form 10-Q

Purchase of property and equipment	(463,807)

Net Cash Used by Investing Activities	(463,807)

Cash Flows From Financing Activities:	
Capital contributions from partners	61,263
Payments on long-term debt	(216,310)

Net Cash Used in Financing Activities	\$ (155,047)

The accompanying notes are an integral part of these consolidated financial statements.

7

CROWN ENERGY CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
[Continued]

	For the Nine September 2001 [unaudited]

Net Increase (Decrease) in Cash:	\$ (2,593,351)
	=====
Cash at Beginning of Period	\$ 2,878,141
	=====
Cash at End of Period	\$ 284,790
	=====
Supplemental Disclosure of Cash Flow Information	
Cash paid during the period:	
Interest	\$ 439,836
	=====
Income taxes	---
	=====

Supplemental Schedule of Non-cash Investing and Financing Activities:
For the period ended September 30, 2001:

The Company acquired property and equipment of \$187,038 with long term debt or capital leases.

For the period ended September 30, 2000:

None

Edgar Filing: CROWN ENERGY CORP - Form 10-Q

The accompanying notes are an integral part of these consolidated financial statements.

8

CROWN ENERGY CORPORATION NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying consolidated financial statements have been prepared by the Company without audit. In the opinion of management, all adjustments (which include only normal recurring adjustments) necessary to present fairly the financial position, results of operations and changes in stockholders' equity and cash flows at September 30, 2001 and for all periods presented have been made.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted. It is suggested that these condensed financial statements be read in conjunction with the financial statements and notes thereto included in the Company's December 31, 2000 Annual Report on Form 10-K. The results of operations for the period ended September 30, 2001 are not necessarily indicative of the operating results for the full year.

Summary of Disputes - The Company and its joint venture partner in Crown Asphalt Distribution, L.L.C. ("Crown Distribution") and Crown Asphalt Ridge, L.L.C. ("Crown Ridge"), MCNIC Pipeline and Processing Company ("MCNIC"), were involved in a dispute relating to Crown Distribution where claims were made by each party against the other. These disputes are discussed in detail in the Company's December 31, 2000 Annual Report on Form 10-K. Binding arbitration of these disputes began on July 23, 2001 before Judge John G. Davies (ret.) in Salt Lake City, Utah. On November 5, 2001, the Company received the decision of the arbitrator in which he ruled that (i) no damages were awarded to the Company for its claims against MCNIC; (ii) the loans made by MCNIC to Crown Distribution are due and payable along with accrued interest; and (iii) Crown Distribution is to pay MCNIC's legal fees and costs associated with the collection of that portion of the loans that were covered by the Promissory Note from MCNIC to Crown Distribution made as part of the purchase of the asphalt assets of Petro Source Asphalt Company in 1998 (the "Petro Source Acquisition"). Interested persons should note the significant and material adverse impacts the Company could experience in the event MCNIC elects to foreclose on the Crown Distribution assets securing the loans.

Organization - Crown Energy Corporation ("CEC") and its wholly-owned subsidiaries, Crown Asphalt Corporation ("CAC") and Crown Asphalt Products Company ("Capco") and Crown Distribution, an entity in which Capco owns a majority interest (collectively referred to as the "Company"), are engaged in the mining, production, manufacturing, distribution and selling of asphalt products.

Majority Owned Subsidiaries - Capco is the majority-owner of Crown Distribution, Crown Distribution is a joint venture limited liability

Edgar Filing: CROWN ENERGY CORP - Form 10-Q

company formed on July 2, 1998 between Capco and MCNIC for the purpose of acquiring certain assets of Petro Source Asphalt Company ("Petro Source"). Capco owns 50.01% and MCNIC owns 49.99% of Crown Distribution. Capco is the general manager and operating agent of Crown Distribution. Crown Distribution owns a majority interest in Cowboy Asphalt Terminal, L.L.C. ("CAT, L.L.C."). CAT LLC is a joint venture formed on June 16, 1998 between Capco and Foreland Asphalt Corporation ("Foreland"), which owns an asphalt terminal and storage facility. Crown Distribution owns 66.67% and Foreland owns 33.33% of CAT LLC.

Principles of Consolidation - The consolidated financial statements include the accounts of the Company and its wholly or majority-owned subsidiaries. All significant inter-company transactions have been eliminated in consolidation.

9

CROWN ENERGY CORPORATION NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 2 - WORKING CAPITAL CREDIT FACILITY

As described in detail in the Company's Annual Report on Form 10-K for the year ended December 31, 2000, the Company maintains that MCNIC, pursuant to its rights granted under the Crown Distribution Operating Agreement, elected to extend a credit facility for working capital purposes (the "Credit Facility"). The Credit Facility, along with a working capital loan (the "Working Capital Loan"), provided by MCNIC in conjunction with the Petro Source Acquisition have a balance of approximately \$14,935,222 plus accrued interest of \$4,414,942 through the period ended September 30, 2001. The decision rendered in final arbitration concluded that all of the foregoing principal amounts, together with accrued interest are now due and payable. The Credit Facility and the Working Capital Loan are secured by the majority of Crown Distribution's assets. As noted elsewhere, significant and materially adverse impacts on the Company would result from MCNIC's foreclosure on Crown Distribution's assets.

NOTE 3 - CAPITAL TRANSACTIONS

Preferred Stock - The Company is authorized to issue 1,000,000 preferred shares, par value \$.005 per share. The Company issued and has outstanding 500,000 shares of its Series A Cumulative Convertible Preferred Stock ("Series A Preferred"). Each share of Series A Preferred is convertible at the option of its holder, at any time, into 8.57 shares of common stock of the Company. Dividends accrue on the outstanding Series A Preferred at the rate of 8% per annum and may be paid through cash or common shares of the Company at the option of the holder. Subject to the holder's right to convert the Series A Preferred, the Company may redeem the Series A Preferred at any time from the date on which it is issued at a percentage of the Series A Preferred's stated value of \$10 per share, 130% of stated value if redemption occurs within thirty-six months of the date of issuance; 115% of stated value if redemption occurs between thirty-six and forty-eight months after the date of issuance; 110% of stated value if redemption occurs between forty-eight and sixty months after the date of issuance; and 100% if redemption occurs thereafter. The holder of the Series A Preferred may also require the Company to redeem the Series A Preferred after the eighth anniversary of the Series A

Edgar Filing: CROWN ENERGY CORP - Form 10-Q

Preferred's issuance. The holders of the Series A Preferred shall have the right, but shall not be obligated, to appoint 20% of the Company's Board of Directors. The Company may not alter the rights and preferences of the Series A Preferred, authorize any security having liquidation preference, redemption, voting or dividend rights senior to the Series A Preferred, increase the number of Series A Preferred, reclassify its securities or enter into specified extraordinary events without obtaining written consent or an affirmative vote of at least 75% of the holders of the outstanding shares of the Series A Preferred stock. All voting rights of the Series A Preferred expire upon the issuance by the Company of its notice to redeem such shares. The shares of common stock issuable upon conversion of the Series A Preferred are subject to adjustment upon the issuance of additional shares of the Company's common stock resulting from stock splits, share dividends, and other similar events as well as upon the issuance of additional shares or options which are issued in connection with the Company's equity investment or as compensation to any employee, director, consultant, or other service provider of the Company or any subsidiary, other than options to acquire up to 5% of the Company's common stock at or less than fair market value.

Common Stock Warrant - In conjunction with the issuance of the preferred stock described above, the Company issued a warrant to the holders of the preferred stock. The fair value of the warrant at the date of issuance was estimated to be \$283,019 and was recorded to additional paid-in capital and as a reduction to the stated value of the preferred stock. The reduction in preferred stock is being accreted over the five-year period from the date of issuance to the earliest exercise date of the warrant. Upon the fifth anniversary of the issuance of the preferred stock, the warrant becomes exercisable, at \$.002 per share, into the number of common shares of the Company equal to (a) [\$5,000,000 plus the product of (i) \$5,000,000 multiplied by (ii) 39% (internal rate of

10

CROWN ENERGY CORPORATION NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

return) multiplied by (iii) 5 years] (14,750,000), minus (b) the sum of (i) all dividends and other distributions paid by the Company on the preferred stock or on the common stock received upon conversion of the preferred stock plus (ii) the greater of the proceeds from the sale of any common stock received by the holder upon the conversion of the preferred stock prior to the fifth anniversary date or the Terminal Value (as defined) of such common stock sold before the fifth anniversary plus (iii) the terminal value of the preferred stock and common stock received upon conversion of the preferred stock then held, divided by (c) the fair market value of the Company's common stock on a weighted average basis for the 90 days immediately preceding the fifth anniversary date of the issuance of the preferred stock. Terminal Value is defined as the sum of (i) the shares of common stock into which the preferred stock then held is convertible, plus (ii) shares of common stock received upon conversion of preferred stock, multiplied by the fair market value of the Company's common stock on a weighted average basis for the 90 days immediately preceding the fifth anniversary date of the issuance of the preferred stock. The warrants will expire in 2007.

Edgar Filing: CROWN ENERGY CORP - Form 10-Q

Net loss attributable to common stockholders	(\$2,742,305) =====	(\$0.20) =====	(\$4,406,085) =====
Weighted average common shares outstanding - basic and diluted	13,635,581 =====		13,289,427 =====

The Company had at September 30, 2001 and September 30, 2000, incremental options and warrants to purchase, computed under the treasury stock method, 3,463,148 and 3,277,148 respectively, shares of common stock that were not included in the computation of diluted earnings (loss) per share because their effect was anti-dilutive. The Company also has preferred stock outstanding at September 30, 2001 and September 30, 2000 which is convertible into approximately 4,300,000 shares of common stock that was not included in the computation of diluted earnings per share as its effect was anti-dilutive. Accordingly, diluted earnings per share does not differ from basic earnings.

12

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

The following discussion and analysis of the Company's financial condition, results of operations and related matters includes a number of forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Forward-looking statements include, by way of illustration and not limitation, statements containing the words "anticipates", "believes", "expects", "intends", "future" and words of similar import which express, either directly or by implication, management's beliefs, expectations or intentions regarding the Company's future performance or future events or trends which may affect the Company or its results of operations.

Forward-looking statements are subject to known and unknown risks, uncertainties and other factors, including but not limited to changes in economic conditions generally or with respect to the Company's asphalt products market in particular, new or increased governmental regulation, increased competition, shortages in labor or materials, delays or other difficulties in shipping or transporting the Company's products, continued or additional technical or operational uncertainties and difficulties at the facility of Crown Asphalt Ridge, L.L.C. ("Crown Ridge"), a determination of what the recently received adverse arbitration decision will mean for the Company and Crown Distribution, difficulties in integrating the Company's recent joint venture and acquisition related businesses and other similar risks inherent in the Company's operations or in business operations generally. Any such risks or uncertainties, either alone or in combination with other factors, may cause the actual results, performance or achievements of the Company to differ materially from its anticipated future results, performance or achievements (which may be expressed or implied by such forward looking statements). Consequently, the following management's discussion and analysis, including all forward-looking statements contained therein, is qualified and limited by the foregoing cautionary factors. Interested persons are advised to consider all forward-looking statements within the context of such cautionary factors.

Edgar Filing: CROWN ENERGY CORP - Form 10-Q

Liquidity and Capital Resources

At September 30, 2001, the Company had cash and other current assets of \$11,283,569 as compared to cash and other current assets of \$6,761,595 at December 31, 2000. The increase of \$4,521,974 was primarily due to the increase in accounts receivable attributable to asphalt sales in the second and third quarter of 2001. The Company's wholly-owned subsidiary, Capco, is the majority owner of Crown Asphalt Distribution, L.L.C. ("Crown Distribution") and also conducts asphalt distribution independent of Crown Distribution. Together Capco and Crown Distribution accounted for most of the Company's cash and other current assets. As of September 30, 2001, Capco and Crown Distribution had cash and other current assets of approximately \$11,098,803 million, consisting primarily of roughly \$232,009 of cash, \$2,338,742 million in inventory and \$8,411,068 million in accounts receivable, excluding related party balances. Capco's and Crown Distribution's businesses are capital intensive and require working capital or some type of a working capital credit facility. MCNIC Pipeline & Processing Company ("MCNIC"), the minority joint venture partner of Crown Distribution, elected to provide the Credit Facility in addition to the Working Capital Loan. As of September 30, 2001, the Company asserts that these loans had an outstanding principal balance of \$14,935,222 and accrued interest of \$4,414,942.

On November 5, 2001, the Company received a decision of the arbitrator in the dispute between the Company and MCNIC where it was ruled that the loans made by MCNIC to Crown Distribution are currently due and payable along with accrued interest. The Company may have to seek replacement financing on terms and conditions, which are less favorable than it might obtain under other circumstances. It is conceivable that MCNIC might obtain possession and legal control over the operating assets of Crown Distribution. Interested persons should note the significant and material risks facing the Company as a result of this development. The Company and Crown Distribution are actively evaluating appropriate courses of action which may be taken in response to this material development.

13

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

Interested persons should also note that, subject of course to available equitable and other creditor remedies, neither the Working Capital Loan or the Credit Facility contain cross-default provisions giving MCNIC any right to declare a default or to seek control or possession over the assets or operations of Crown Ridge or the Company's interest in Crown Ridge, or other assets of the Company.

Crown Distribution also owed MCNIC an additional \$5,325,723 at September 30, 2001 with respect to the preferential capital contribution (the "Preferred Contribution") that funded Crown Distribution's acquisition of the assets of Petro Source Asphalt Company on July 2, 1998. The Preferred Contribution accrues a 15% annual rate of return and is payable solely from 50% of the cash flow, if any, from Crown Distribution's operations.

The asphalt distribution business is seasonal in nature and necessitates working capital financing for inventory purchases, receivables and operations. It is capital intensive and requires substantial investments to acquire terminal storage, blending, and raw material assets. MCNIC has advised the Company it will no longer provide funding under the Credit Facility and has refused to jointly and severally guaranty working capital financing from a third party on behalf of Crown Distribution, as the Company believes MCNIC has also

Edgar Filing: CROWN ENERGY CORP - Form 10-Q

previously agreed. The Company relies on working capital financing to purchase inventory and fund other working capital requirements for operations. The Company is seeking other ways to finance its working capital requirements, but there is no assurance that such working capital financing can be secured by the Company.

In the event that the Company is unable to collect its current accounts receivables, or the Company is unable to secure the necessary working capital financing for its operations from third party sources or if the Company's operating losses and working capital deficits continue, or if the Company is unable to recoup the losses, the Company may not have sufficient capital to continue to operate its business. Thus, the risk exists that the Company may not be able to continue as a going concern.

The Company remains open to other asphalt related business opportunities to complement its existing asphalt distribution capabilities. There can be no assurance, however, that the Company can obtain the additional capital financing required for such transactions on acceptable terms and conditions.

As has been previously disclosed by the Company in its periodic filings, the tar sands processing facility owned by Crown Ridge has not commenced commercial operations due to mechanical and process difficulties experienced during start-up of the facilities. A pilot study to develop a solution to these problems was conducted during fiscal year 2000. The ramifications of the pilot study for the Company are uncertain in that the cost of the modifications which need to be made to the Crown Ridge facility and its commercial viability have not been determined.

Due to the inherent risks of arbitration involved in the Company's disputes with MCNIC and the lack of a firm business plan for Asphalt Ridge from MCNIC, the Company determined that its investment in, and advances to, Crown Ridge are potentially impaired. Should delays continue, or should the Crown Ridge facility be unable to ever operate economically, the Company believes that this would significantly impact Crown Ridge's ability to continue as a going concern and would adversely impact the Company's operations and financial conditions resulting in an impairment of the remainder of the asset. Further, although the pilot study may demonstrate that the mechanical process difficulties experienced by the Crown Ridge facility can be resolved, there can be no assurance that the Company will be able to make the proportionate capital contribution which would be necessary to finance its approximate 24% of the costs involved. Accordingly, it is possible that the Company's sharing ratio in Crown Ridge may be further diluted should it agree to proceed with further expenditures.

14

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

Results of Operations

For the three month period ending September 30, 2001 compared to the three month period ending September 30, 2000

Total revenue increased from \$11,556,473 for the three month period ended September 30, 2000 to \$15,539,700 for the three month period ended September 30, 2001, an increase of \$3,983,227. Cost of sales increased from \$11,400,727 for the same period in 2000 to \$12,757,549 for the same period in 2001, a increase of \$1,356,822. The increase in revenues is primarily due to an

Edgar Filing: CROWN ENERGY CORP - Form 10-Q

increase in asphalt sales volume of approximately 38% in the third quarter of 2001. The increase in cost of sales is primarily the result of increased volume, offset partially by reduced base asphalt purchase costs of approximately 16% and operating efficiencies at the distribution facilities.

General and administrative expenses increased from \$649,608 for the three month period ended September 30, 2000 to \$926,719 for the three month period ended September 30, 2001, an increase of \$277,111. This increase is primarily due to increased legal expenses.

Other income/expenses increased from \$557,316 for the three month period ended September 30, 2000 to \$1,812,657 for the three month period ended September 30, 2001, an increase of \$1,255,341. The 2001 total is comprised of \$502,514 interest related to the Company's Credit Facility, Working Capital Loan and Preferred Contribution for its asphalt distribution business, \$1,164,574 of interest related to the arbitration judgment, and other interest costs of \$150,446. This amount is partially offset by interest income and other income of \$4,877.

Minority interest of \$2,930 represents Foreland's approximate 33% interest in the loss of CAT, LLC.

For the nine month period ending September 30, 2001 compared to the nine month period ending September 30, 2000

Total revenue increased from \$19,745,578 for the period ended September 30, 2000 to \$23,185,290 for the period ended September 30, 2001, a increase of \$3,439,712. Cost of sales also increased from \$20,101,720 for the period ended September 30, 2000 to \$20,331,211 for the period ended September 30, 2001, a increase of \$229,491. The increase in revenues was primarily due to an increase in asphalt sales volume of approximately 18%. The increase in cost of sales is primarily the result of increased volume, offset partially by lower asphalt purchase prices of approximately 13% and operating efficiencies at the distribution facilities.

General and administrative expenses increased from \$1,743,465 for the period ended September 30, 2000 to \$2,518,780 for the period ended September 30, 2001, an increase of \$775,315. This increase is primarily due to two factors: (i) the prior year's amount was reduced by \$320,000, which represented a receivable collection that had previously been written off as a bad debt, and (ii) increased legal expenses.

Other income/expenses increased from \$1,985,435 for the period ended September 30, 2000 to \$2,749,283 for the period ended September 30, 2001, an increase of \$763,848. The 2001 total was comprised of \$1,491,160 interest related to the Company's Credit Facility, Working Capital Loan and Preferred Contribution for its asphalt distribution business, \$1,164,574 interest related to the Arbitration Decision, and other interest costs of \$439,836. This amount is partially offset by an insurance settlement gain of \$278,492 and interest income and other income of \$67,795.

Minority interest of \$14,132 represents Foreland's approximate 33% interest in the loss of CAT, LLC.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company does not believe it is subject to the material risks of

Edgar Filing: CROWN ENERGY CORP - Form 10-Q

loss related to certain market risks, such as interest rate risks, foreign currency exchange rate risks or similar risks, and therefore the Company does not engage in transactions, such as hedging or similar transactions in derivative financial instruments, intended to reduce its exposure to such risks. However, the Company is subject to general market fluctuations related to the purchase of its basestock asphalt and may suffer reduced operating margins to the extent its increased costs are not passed through to its customers. Such prices generally fluctuate with the price of crude oil. The Company is prevented in certain contracts with MCNIC from utilizing any hedging strategies to minimize any market price changes. The Company believes the inability to protect itself from market fluctuations may negatively impact its profit margins.

The Company is also subject to certain price escalation and de-escalation clauses in its asphalt distribution sales contracts. The Company supplies asphalt to projects in certain states where regulations provide for escalation and de-escalation of the price for such asphalt relative to the price difference from the time the project is awarded to the successful bidding company and the time the project is completed. The Company includes such de-escalation risk into its bid process and does not believe it has material exposure to risk resulting from these regulations.

16

PART II - OTHER INFORMATION

ITEM 1. Legal Proceedings

As discussed within the Company's Report on Form 10-K for the fiscal year ended December 31, 2000, the Company was engaged in an extensive dispute with MCNIC, MCN and related parties. On November 5, 2001, the Company received a decision in the arbitration between the Company and MCNIC that was issued by the Honorable John G. Davies, U.S. District Judge (ret.) (the "Decision"). The Decision held that loans from MCNIC to Crown Distribution totaling \$14,935,221 were now due and payable, with interest accruing on such loans from 8% to 18%, depending upon the particular loan involved. The Company had not disputed the existence of the loans, but had argued that they were part of a working capital facility extended by MCNIC which was not due and payable at this time. The foregoing loans are secured by a majority of the real and personal property of Crown Distribution. The Decision also failed to find for the Company on its claims against MCN and MCNIC on a number of causes of action. Crown Distribution was also ordered to pay MCN and MCNIC attorneys fees and costs associated with the collection of that portion of the loans that were covered by the Promissory Note from MCNIC to Crown Distribution made as part of the Petro Source Acquisition. The amount of such costs is unknown at the present time. The Company is currently assessing the impact of the decision on Crown Distribution's business and evaluating appropriate courses of action.

On July 14, 1999, Crown Distribution and Capco filed an action in the United States District Court for the Central District of California, Southern Division, against Santa Maria Refining Company ("SMRC"), SABA Petroleum Company ("SABA") and Greka Energy Corporation ("Greka"). The claims include causes of action for breach of contract, breach of the covenant of good faith and fair dealing, conversion, fraud, claim and delivery, unjust enrichment and constructive trust, unfair competition, declaratory relief and specific performance. These claims arise out of the alleged termination of the Processing Agreement and subsequent refusal to deliver asphalt to Crown Distribution by SMRC, SABA, and Greka. A final settlement was reached effective October 23, 2001 in the litigation between the Company and SMRC, SABA and Greka. The Settlement Agreement between the parties requires that the terms of the settlement not be disclosed, but the Company believes the matter was amicably resolved on terms

Edgar Filing: CROWN ENERGY CORP - Form 10-Q

believed to be mutually beneficial to all of the parties.

On January 25, 2000, Oriental New Investments, Ltd. ("Oriental") filed a Complaint against the Company in the Third Judicial District Court, Salt Lake County, Utah. The action relates to a 1997 convertible debenture and replacement convertible debenture issued by the Company to Oriental. The action seeks to recover from the Company \$50,000 liquidated damages, plus interest, and attorneys fees and costs, for alleged breaches of certain terms of the convertible debentures. The Company answered the Complaint on March 1, 2000, denying any and all liability, and believes that Oriental's claims are meritless. On August 17, 2001 the Complaint was dismissed.

ITEM 2. Changes in Securities

None.

ITEM 3. Defaults upon Senior Securities

The Decision in the arbitration of the dispute between the Company and MCNIC received on November 5, 2001 held that loans from MCNIC to Crown Distribution were due and payable, along with accrued interest, and are in default. As of September 30, 2001, the Company asserts that these loans had an outstanding principal balance of \$14,935,222 and accrued interest of \$4,414,942. See "Part I - Item 2: Management's Discussion and Analysis of Financial Condition and Results of Operations; Part II - Item 1: Legal Proceedings."

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

None

ITEM 5. Other Information

None.

17

PART II - OTHER INFORMATION (Continued)

ITEM 6. Exhibits and Reports on Form 8-K

The Company filed a Form 8-K on October 31, 2001 to report that on October 23, 2001 a final settlement had been reached in the litigation between the Company and Santa Maria Refining Company, Saba Petroleum Company and Greka Energy Corporation.

The company also filed a Form 8-K on November 6, 2001 to report that a decision had been reached in the arbitration between the Company and MCNIC.

18

PART III - SIGNATURES

Pursuant to the requirements 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.

CROWN ENERGY CORPORATION
(Registrant)

Edgar Filing: CROWN ENERGY CORP - Form 10-Q

Date: November 14, 2001

By: /s/ Jay Mealey

Jay Mealey, Chief Executive Officer

Date: November 14, 2001

By: /s/ Alan Parker

Alan Parker, Controller