

ROYALE ENERGY INC
Form 10-Q/A
August 05, 2010

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q/A
Amendment No. 1 to
QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(D)
OF THE SECURITIES EXCHANGE ACT OF 1934

For the Quarterly Period Ended March 31, 2010 Commission File No. 000-22750

ROYALE ENERGY, INC.
(Exact name of registrant as specified in its charter)

California 33-0224120
(State or other (I.R.S. Employer
jurisdiction of Identification No.)
incorporation or
organization)

7676 Hazard Center Drive, Suite 1500
San Diego, CA 92108
(Address of principal executive offices)
(Zip Code)
619-881-2800
(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Check one:
Large accelerated filer Accelerated filer
Non-accelerated filer Smaller reporting company

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

At March 31, 2010, a total of 10,243,066 shares of registrant's common stock were outstanding.

Introductory Note

This amendment to Royale Energy's quarterly report on Form 10-Q contains a restatement of a portion of its financial statements to account for available for sale securities. Royale Energy acquired shares of a start-up company's common stock in 2000 in settlement of a legal claim (the "Settlement Stock"). At the time of the acquisition, there was no resale market for the Settlement Stock, and its value was undeterminable. In September 2009, the issuer of the Settlement Stock conducted an initial public offering of its stock, and a market for the Settlement Stock was established. Royale Energy did not receive timely notice of the completion of the public offering and did not, until June 2010, become aware that a public market for the Settlement Stock existed.

Because an ascertainable market price of the Settlement Stock existed at March 31, 2010, the Settlement Stock has been classified as available for sale securities as of that date. The classification caused an adjustment on the Balance Sheet as of March 31, 2010, as follows:

- Total Current Assets and Total Assets of the Company were adjusted upward by approximately \$1.16 million; and
- Approximately \$429,000 was recorded under Current Liabilities as Current Portion of Deferred Tax Liability, and approximately \$728,000 was recorded under Stockholders' Equity as Accumulated Other Comprehensive Income (Loss).

The restatement resulted in recording an increase in unrealized holding gain of \$156,480 for the three months ended March 31, 2010, in Other Comprehensive Income of the Company's Statement of Operations, but no change occurred in the Company's Net Income (Loss) or Earnings per Share as a result of the restatement. See, the Company's Unaudited Financial Statements – Balance Sheets, pages 1-2, Statements of Operations, page 3, and Note 7 – Fair Value Measurements, pages 10-11.

This amendment on Form 10-Q/A contains no changes other than those described above.

TABLE OF CONTENTS

| | | |
|---------|---|----|
| PART I | FINANCIAL INFORMATION | 1 |
| Item 1. | Financial Statements | 1 |
| Item 2. | Management's Discussion and Analysis of Financial Condition and Results of Operations | 12 |
| Item 3 | Quantitative and Qualitative Disclosures About Market Risk | 14 |
| Item 4 | Controls and Procedures | 15 |
| PART II | OTHER INFORMATION | 15 |
| Item 1 | Legal Proceedings | 15 |
| Item 1A | Risk Factors | 15 |
| Item 6. | Exhibits | 15 |
| | Signatures | 16 |

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

ROYALE ENERGY, INC.
BALANCE SHEETS

| | March 31, 2010 (Unaudited) | December 31, 2009 (Audited) |
|--|----------------------------------|-----------------------------------|
| ASSETS | | |
| Current Assets | | |
| Cash and Cash Equivalents | \$2,968,506 | \$3,835,282 |
| Accounts Receivable | 2,255,740 | 2,493,108 |
| Prepaid Expenses | 573,032 | 842,226 |
| Available for Sale Securities | 1,156,800 | 1,000,320 |
| Inventory | 845,874 | 845,874 |
| Total Current Assets | 7,799,952 | 9,016,810 |
| Other Assets | | |
| Other Assets | 6,946 | 6,946 |
| Deferred Tax Asset-Noncurrent | 5,960,403 | 5,740,414 |
| Oil and Gas Properties, at cost, (successful efforts basis), | | |
| Equipment and Fixtures | 9,036,537 | 8,800,293 |
| Total Assets | \$22,803,838 | \$23,564,463 |

See notes to unaudited financial statements

ROYALE ENERGY, INC.
BALANCE SHEETS

| | March 31, 2010 (Unaudited) | December 31, 2009 (Audited) |
|---|----------------------------------|-----------------------------------|
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current Liabilities: | | |
| Accounts Payable and Accrued Expenses | \$4,727,319 | \$5,128,987 |
| Current Portion of Long-Term Debt | 36,667 | 50,417 |
| Current Portion of Deferred Tax Liability | 429,173 | 323,757 |
| Deferred Revenue from Turnkey Drilling | 4,935,200 | 4,979,605 |
| Total Current Liabilities | 10,128,359 | 10,482,766 |
| Noncurrent Liabilities: | | |
| Asset Retirement Obligation | 544,704 | 514,361 |
| Long-Term Debt, Net of Current Portion | 2,280,000 | 2,440,000 |
| Total Noncurrent Liabilities | 2,824,704 | 2,954,361 |
| Total Liabilities | 12,953,063 | 13,437,127 |
| Stockholders' Equity: | | |
| Common Stock, no par value, authorized 20,000,000 shares, 10,275,685 and 10,257,827 shares issued; 10,243,066 and 10,225,208 shares outstanding, respectively | 27,246,740 | 27,246,740 |
| Convertible preferred stock, Series AA, no par value, 147,500 shares authorized; 52,784 and 52,784 shares issued and outstanding, respectively | 154,014 | 154,014 |
| Accumulated Deficit | (18,487,967) | (18,115,452) |
| Accumulated Other Comprehensive Income (Loss) | 727,627 | 676,563 |
| Total Paid in Capital and Accumulated Deficit | 9,640,414 | 9,961,865 |
| Less Cost of Treasury Stock 32,619 and 32,619 shares | (179,376) | (179,376) |
| Additional Paid in Capital | 389,737 | 344,847 |
| Total Stockholders' Equity | 9,850,775 | 10,127,336 |
| Total Liabilities and Stockholders' Equity | \$22,803,838 | \$23,564,463 |

See notes to unaudited financial statements

ROYALE ENERGY, INC.
STATEMENTS OF OPERATIONS
FOR THE QUARTER ENDED MARCH 31, 2010 AND 2009

| | 2010 (Unaudited) | 2009 (Unaudited) |
|--|---------------------|---------------------|
| Revenues: | | |
| Sale of Oil and Gas | \$ 790,781 | \$ 838,577 |
| Turnkey drilling | 724,828 | 1,290,467 |
| Supervisory Fees and Other | 133,370 | 139,126 |
| Total Revenues | 1,648,979 | 2,268,170 |
| Costs and Expenses: | | |
| General and Administrative | 941,045 | 903,782 |
| Turnkey Drilling and Development | 454,086 | 1,220,694 |
| Lease Operating | 258,409 | 446,938 |
| Bad Debt Expense | 0 | 15,865 |
| Legal and Accounting | 191,997 | 366,511 |
| Marketing | 150,752 | 212,707 |
| Depreciation, Depletion and Amortization | 239,685 | 542,775 |
| Total Costs and Expenses | 2,235,974 | 3,709,272 |
| Income (Loss) From Operations | (586,995) | (1,441,102) |
| Other Expense: | | |
| Interest expense | 5,509 | 18,961 |
| Income (Loss) Before Income Tax Expense | (592,504) | (1,460,063) |
| Income Tax Provision (Benefit) | (219,989) | (569,007) |
| Net Income (Loss) | \$ (372,515) | \$ (891,056) |
| Basic Earnings Per Share: | | |
| Net Income available to common stock | \$ (0.04) | \$ (0.10) |
| Diluted Earnings Per Share | \$ (0.04) | \$ (0.10) |
| Other Comprehensive Income | | |
| Unrealized Gain (Loss) on Equity Securities | \$ 156,480 | \$ 31,014 |
| Other Comprehensive Income (Loss), before tax | 156,480 | 31,014 |
| Income Tax Expense (Benefit) Related to Items of Other Comprehensive Income | 105,416 | 13,688 |

Edgar Filing: ROYALE ENERGY INC - Form 10-Q/A

| | | |
|--|--------------|--------------|
| Other Comprehensive Income, net of tax | 51,064 | 17,326 |
| Comprehensive Income (Loss) | \$ (321,451) | \$ (873,730) |

See notes to unaudited financial statements

-3-

ROYALE ENERGY, INC.
STATEMENTS OF CASH FLOWS
FOR THE QUARTER ENDED MARCH 31, 2010 AND 2009

| | 2010 (Unaudited) | 2009 (Unaudited) |
|--|---------------------|---------------------|
| CASH FLOWS FROM OPERATING ACTIVITIES | | |
| Net Income (Loss) | \$(372,515) | \$(891,056) |
| Adjustments to Reconcile Net Loss to Net Cash Used by Operating Activities: | | |
| Depreciation, Depletion and Amortization | 239,685 | 542,775 |
| Bad Debt Expense | 0 | 15,865 |
| Stock-Based Compensation, net of adjustments | 44,890 | 39,376 |
| (Increase) Decrease in: | | |
| Accounts Receivable | 237,368 | 1,577,003 |
| Prepaid Expenses and Other Assets | 269,194 | 832,773 |
| Increase (Decrease) in: | | |
| Accounts Payable and Accrued expenses | (371,325) | (2,074,284) |
| Deferred Revenues - DWI | (44,405) | 3,780 |
| Deferred Income Taxes | (219,989) | (611,912) |
| Net Cash Used by Operating Activities | (217,097) | (565,680) |
| CASH FLOWS FROM INVESTING ACTIVITIES | | |
| Expenditures for Oil and Gas Properties and Other Capital Expenditures | (475,929) | (190,959) |
| Proceeds from Sale of Assets | 0 | 0 |
| Purchase of Equity Securities | 0 | (7,991) |
| Net Cash Used by Investing Activities | (475,929) | (198,950) |
| CASH FLOWS FROM FINANCING ACTIVITIES | | |
| Proceeds from Long-Term Debt | 2,280,000 | 4,454,181 |
| Principal Payments on Long-Term Debt | (2,453,750) | (1,975,974) |
| Net Cash Provided (Used) by Financing Activities | (173,750) | 2,478,207 |
| Net Increase (Decrease) in Cash and Cash Equivalents | (866,776) | 1,713,577 |
| Cash at Beginning of Year | 3,835,282 | 1,330,739 |
| Cash at End of Period | \$2,968,506 | \$3,044,316 |
| SUPPLEMENTAL DISCLOSURES OF CASH FLOWS INFORMATION: | | |
| Cash Paid for Interest | \$2,825 | \$18,961 |

| | | |
|---------------------|---------|----------|
| Cash Paid for Taxes | \$4,168 | \$42,905 |
|---------------------|---------|----------|

See notes to unaudited financial statements

ROYALE ENERGY, INC.
NOTES TO UNAUDITED FINANCIAL STATEMENTS

NOTE 1 – In the opinion of management, the accompanying unaudited financial statements include all adjustments, consisting only of normally recurring adjustments, necessary to present fairly the Company’s financial position and the results of its operations and cash flows for the periods presented. The results of operations for the three month period are not, in management’s opinion, indicative of the results to be expected for a full year of operations. It is suggested that these financial statements be read in conjunction with the financial statements and the notes thereto included in the Company’s latest annual report.

NOTE 2 – EARNINGS PER SHARE

Basic and diluted earnings (loss) per share are calculated as follows:

| | For the Three Months ended March 31, 2010 | | |
|---|--|-------------------------|---------------------|
| | Income (Numerator) | Shares (Denominator) | Per-Share Amount |
| Basic Earnings (Loss) Per Share: | | | |
| Net income available to common stock | \$ (372,515) | 10,240,487 | \$(0.04) |
| Diluted Earnings (Loss) Per Share: | | | |
| Effect of dilutive securities and stock options | 0 | 0 | 0.00 |
| Net income available to common stock | \$(372,515) | 10,240,487 | \$(0.04) |
| | For the Three Months ended March 31, 2009 | | |
| | Income (Numerator) | Shares (Denominator) | Per-Share Amount |
| Basic Earnings (Loss) Per Share: | | | |
| Net income available to common stock | \$ (891,056) | 8,506,098 | \$(0.10) |
| Diluted Earnings (Loss) Per Share: | | | |
| Effect of dilutive securities and stock options | 0 | 0 | 0.00 |
| Net income available to common stock | \$(891,056) | 8,506,098 | \$(0.10) |

For the three months ended March 31, 2010 and 2009, Royale Energy had dilutive securities of 889,128 and 26,392, respectively. These securities were not included in the dilutive loss per share due to their anti-dilutive nature.

ROYALE ENERGY, INC.
NOTES TO UNAUDITED FINANCIAL STATEMENTS

NOTE 3 – OIL AND GAS PROPERTIES, EQUIPMENT AND FIXTURES

Oil and gas properties, equipment and fixtures consist of the following:

| | March 31, 2010 | December 31, 2009 |
|--|-------------------|----------------------|
| Oil and Gas | | |
| Producing properties, including drilling costs | \$24,036,231 | \$23,746,696 |
| Undeveloped properties | 613,979 | 570,831 |
| Lease and well equipment | 9,363,411 | 9,251,307 |
| | 34,013,621 | 33,568,834 |
| Accumulated depletion, depreciation & amortization | (25,709,706) | (25,512,869) |
| | 8,303,915 | 8,055,965 |
| Commercial and Other | | |
| Real estate, including furniture and fixtures | \$502,344 | \$502,344 |
| Vehicles | 255,496 | 255,496 |
| Furniture and equipment | 1,263,444 | 1,258,439 |
| | 2,021,284 | 2,016,279 |
| Accumulated depreciation | (1,288,662) | (1,271,951) |
| | 732,622 | 744,328 |
| | \$9,036,537 | \$8,800,293 |

The guidance set forth in the Continued Capitalization of Exploratory Well Costs paragraph of the Extractive Activities Topic of the FASB Accounting Standards Codification (ASC) requires that we evaluate all existing capitalized exploratory well costs and disclose the extent to which any such capitalized costs have become impaired and are expensed or reclassified during a fiscal period. We did not make any additions to capitalized exploratory well costs pending a determination of proved reserves during 2010 or 2009.

| | Three Months ended March 31, | |
|---|---------------------------------|------|
| | 2010 | 2009 |
| Beginning balance at January 1 | \$0 | \$0 |
| Additions to capitalized exploratory well costs pending the determination of proved reserves | 312,376 | 0 |
| Reclassifications to wells, facilities, and equipment based on the determination of proved reserves | (312,376) | (0) |
| Ending balance at March 31 | \$0 | \$0 |

ROYALE ENERGY, INC.
NOTES TO UNAUDITED FINANCIAL STATEMENTS

NOTE 4 – STOCK BASED COMPENSATION

Royale Energy has a stock-based employee compensation plan. Effective January 1, 2006, the Company adopted the Compensation – Stock Compensation Topic of the FASB ASC, which addresses the accounting for stock-based payment transactions in which an enterprise receives employee services in exchange for (a) equity instruments of the enterprise or (b) liabilities that are based on the fair value of the enterprise's equity instruments or that may be settled by the issuance of such equity instruments. The Company uses the Black-Scholes option-pricing model to determine the fair-value of stock-based awards, consistent with that used for pro forma disclosures under the Topic.

During the March 2008 Board of Directors meeting, directors and executive officers of Royale Energy were each granted 45,000 options, a total of 360,000 options, to purchase common stock at an exercise or base price of \$3.50 per share. These options are to be vested in three parts with 120,000 vesting on March 31, 2008, 2009, and 2010, respectively. The options were granted for a legal life of four years with a service period of three years. Royale Energy recorded compensation expense of \$18,687 in the first quarter of 2010 and 2009 relating to these options. The total income tax benefits recognized in the income statement for these option arrangements were \$6,933 in 2010 and \$7,269 in 2009.

In November 2008, the Board of Directors granted the directors and executive officers of Royale Energy 95,000 shares of restricted common stock. The number of granted shares will double to 190,000 shares of common stock if Royale's stock price reaches \$15 a share during the period. The grant is to be vested in three parts; 31,667 or 63,334 shares, depending on Royale's stock price, will vest on November 30, 2010 and 2011. The first 31,665 shares vested on November 30, 2009. Royale has recognized share-based compensation expense of \$26,203 and \$9,721 as a tax benefit in the first quarter of 2010 relating to this grant. During the same time period in 2009, Royale recognized \$20,689 in compensation expense resulting in a \$8,048 tax benefit relating to this stock grant.

ROYALE ENERGY, INC.
NOTES TO UNAUDITED FINANCIAL STATEMENTS

NOTE 5 – RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

The Company has adopted the Subsequent Events Topic of the FASB Accounting Standards Codification. It establishes general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued. The Topic sets forth (1) The period after the balance sheet date during which management of a reporting entity should evaluate events or transactions that may occur for potential recognition or disclosure in the financial statements, (2) The circumstances under which an entity should recognize events or transactions occurring after the balance sheet date in its financial statements and (3) The disclosures that an entity should make about events or transactions that occurred after the balance sheet date. The Topic is effective for interim or annual financial periods ending after June 15, 2009. The adoption of this standard did not have a significant impact on the Company's interim financial information.

In June 2009, the Financial Accounting Standards Board issued Generally Accepted Accounting Principles Topic of the FASB Accounting Standards Codification. The Topic sets forth that the Financial Accounting Standards Board Accounting Standards Codification is the exclusive authoritative reference for nongovernmental U.S. GAAP for use in financial statements issued for interim and annual periods ending after September 15, 2009, except for SEC rules and interpretive releases, which also are authoritative GAAP for SEC registrants. The change was established by FASB Statement of Financial Accounting Standards No. 168 "The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles" (FAS 168), which divides nongovernmental U.S. GAAP into the authoritative Codification and guidance that is nonauthoritative, doing away with the previous four-level hierarchy. The Topic is effective for financial statements for interim or annual reporting periods ending after September 15, 2009. The Topic was not intended to change or alter existing GAAP, and the Company's adoption did not have any impact on its consolidated financial statements other than to modify certain existing disclosures. Upon adoption, the Company began to use the new guidelines and numbering system prescribed by the Topic when referring to GAAP in the third quarter of fiscal year 2009.

SEC Rulemaking

On December 31, 2008, the SEC published the final rules and interpretations updating its oil and gas reporting requirements. Many of the revisions are updates to definitions in the existing oil and gas rules to make them consistent with the petroleum resource management system, which is a widely accepted standard for the management of petroleum resources that was developed by several industry organizations. Key revisions include the ability to include nontraditional resources in reserves, the use of new technology for determining reserves, permitting disclosure of probable and possible reserves, and changes to the pricing used to determine reserves in that companies must use a 12-month average price. The average is calculated using the first-day-of-the-month price for each of the 12 months that make up the reporting period. The SEC will require companies to comply with the amended disclosure requirements for registration statements filed after January 1, 2010, and for annual reports for fiscal years ending on or after December 15, 2009. The adoption of this rule did not have a significant impact on the Company's financial statements.

NOTE 6 – FINANCIAL INFORMATION RELATING TO INDUSTRY SEGMENTS

Royale Energy identifies reportable segments by product and country, although Royale Energy currently does not have foreign country segments. Royale Energy includes revenues from both external customers and revenues from transactions with other operating segments in its measure of segment profit or loss. Royale Energy also includes interest revenue and expense, DD&A, and other operating expenses in its measure of segment profit or loss.

Royale Energy's operations are classified into two principal industry segments. Following is a summary of segmented information for the three months ended March 31, 2010, and 2009:

| | Oil and Gas Producing and Exploration | Turnkey Drilling Services | Total |
|---------------------------------------|--|---------------------------------|---------------|
| Three Months Ended March 31, 2010: | | | |
| Revenues from External Customers | \$ 790,781 | \$ 724,828 | \$ 1,515,609 |
| Supervisory Fees | \$ 131,131 | \$ 0 | \$ 131,131 |
| Interest Revenue | \$ 0 | \$ 2,239 | \$ 2,239 |
| Interest Expense | \$ 2,755 | \$ 2,754 | \$ 5,509 |
| Expenditures for Segment Assets | \$ 926,904 | \$ 1,069,385 | \$ 1,996,289 |
| DD&A | \$ 227,701 | \$ 11,984 | \$ 239,685 |
| Income Tax (Benefit) | \$ (87,419) | \$ (132,570) | \$ (219,989) |
| Total Assets | \$ 22,803,838 | \$ 0 | \$ 22,803,838 |
| Net Loss | \$ (148,029) | \$ (224,486) | \$ (372,515) |

| | Oil and Gas Producing and Exploration | Turnkey Drilling Services | Total |
|---------------------------------------|--|---------------------------------|---------------|
| Three Months Ended March 31, 2009: | | | |
| Revenues from External Customers | \$ 838,577 | \$ 1,290,467 | \$ 2,129,044 |
| Supervisory Fees | \$ 138,357 | \$ 0 | \$ 138,357 |
| Interest Revenue | \$ 0 | \$ 769 | \$ 769 |
| Interest Expense | \$ 9,481 | \$ 9,480 | \$ 18,961 |
| Expenditures for Segment Assets | \$ 1,205,771 | \$ 1,960,726 | \$ 3,166,497 |
| DD&A | \$ 515,636 | \$ 27,139 | \$ 542,775 |
| Income Tax (Benefit) | \$ (284,504) | \$ (284,503) | \$ (569,007) |
| Total Assets | \$ 23,763,946 | \$ 0 | \$ 23,763,946 |
| Net Loss | \$ (469,450) | \$ (421,606) | \$ (891,056) |

NOTE 7 – FAIR VALUE MEASUREMENTS

According to Fair Value Measurements and Disclosures Topic of the FASB Accounting Standards Codification, assets and liabilities that are measured at fair value on a recurring and nonrecurring basis in period subsequent to initial recognition, the reporting entity shall disclose information that enable users of its financial statements to assess the inputs used to develop those measurements and for recurring fair value measurements using significant unobservable inputs, the effect of the measurements on earnings for the period.

In January 2000, Royale Energy received 96,000 shares (as adjusted for a later stock split) in a new start up company (the "Settlement Stock") as part of a settlement in an action filed against a former consultant. At the time of the settlement, the value of the Settlement Stock was undeterminable because there was no market for the start-up's stock. In September 2009, issuer of the Settlement Stock conducted an initial public offering of stock, and a market for its shares was established. At March 31, 2010, the fair value of these shares was \$1,156,800 and they were classified as available for sale securities. The fair value was determined using the number of shares owned as of the last day of the reporting period multiplied by the market price of those securities on that day. At March 31, 2009, Royale Energy reported the fair value of \$257,943 in available for sale securities. For the purposes of identifying related costs to its available for sale securities, the Company uses a specific identification method. On March 31, 2009, the total cost for those securities amounted to \$458,804. For the quarter ended March 31, 2010 and 2009, unrealized holding gains of \$51,064 and \$17,326, respectively were recorded in the other comprehensive income (loss) section of the Statement of Operations. These unrealized holding gains included the income tax effect of \$105,416 and \$13,688, respectively.

The table below summarizes Royale's fair value measurements and the level within the fair value hierarchy in which the fair value measurements fall:

| Description | March 31, 2010 | Level 1 | March 31, 2009 | Level 1 |
|-------------------------------|-------------------|-------------|-------------------|-----------|
| Available for Sale Securities | \$1,156,800 | \$1,156,800 | \$257,943 | \$257,943 |

-11-

Item 2. Management's Discussion And Analysis Of Financial Condition And Results Of Operations

Forward Looking Statements

In addition to historical information contained herein, this discussion contains "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995, subject to various risks and uncertainties that could cause our actual results to differ materially from those in the "forward-looking" statements. While we believe our forward looking statements are based upon reasonable assumptions, there are factors that are difficult to predict and that are influenced by economic and other conditions beyond our control. Investors are directed to consider such risks and other uncertainties discussed in documents filed by the company with the Securities and Exchange Commission.

Results of Operations

For the first quarter of 2010, we had a net loss of \$372,515 compared to the net loss of \$891,056 during the first quarter of 2009, a \$518,541 improvement. Total revenues for the first quarter in 2010 were \$1,648,979, a decrease of \$619,191 or 27.3% from the total revenues of \$2,268,170 during the period in 2009. This decrease in revenues was the result of a reduction in oil and natural gas production compounded by decreased turnkey drilling revenue due to drilling one less well in the first quarter of 2010 than in 2009. However, Royale was able to reduce the company's quarterly net loss by cutting back total expenses.

In the first quarter of 2010, revenues from oil and gas production decreased \$47,796 or 5.7% to \$790,781 from the 2009 first quarter revenues of \$838,577, due to lower oil and natural gas production, which was partially offset by higher sales prices. The net sales volume of natural gas for the quarter ended March 31, 2010, was approximately 125,826 Mcf with an average price of \$5.27 per Mcf, versus 176,928 Mcf with an average price of \$4.38 per Mcf for the first quarter of 2009. This represents a decrease in net sales volume of 51,102 Mcf or 28.9%. This decrease was mainly due to the natural declines in production from existing wells. The net sales volume for oil and condensate (natural gas liquids) production was 1,839 barrels with an average price of \$69.71 per barrel for the first three months of 2010, compared to 2,002 barrels at an average price of \$32.10 per barrel for the three months in 2009. This represents a decrease in net sales volume of 163 barrels, or 8.1%.

Oil and natural gas lease operating expenses decreased by \$188,529 or 42.2%, to \$258,409 for the quarter ended March 31, 2010, from \$446,938 for the quarter in 2009. This decrease was mainly due to lower workover costs, lower production, and other reduced lease operating costs during the period in 2010.

For the quarter ended March 31, 2010, turnkey drilling revenues decreased \$565,639 or 43.8% to \$724,828 from \$1,290,467 in the same quarter in 2009. We also had a \$766,608 or 62.8% decrease in turnkey drilling and development costs to \$454,086 in 2010 from \$1,220,694 in 2009. Due to greater than normal rain fall during the first three months of 2010, Royale only finished drilling one well in Northern California, the Vann #1, to which Royale is currently in the process of building a pipeline. As the result, turnkey drilling revenues and costs decreased during the period in 2010. Two wells were drilled during the same period in 2009. Thus far in 2010, we have processed permits on several wells in California, and we expect to participate in the drilling of approximately four wells during the second quarter of 2010.

The aggregate of supervisory fees and other income was \$133,370 for quarter ended March 31, 2010, a decrease of \$5,756 (4.1%) from \$139,126 during the period in 2009. This decrease was the result of lower cost recovery fees on facilities due to lower natural gas production.

Depreciation, depletion and amortization expense decreased to \$239,685 from \$542,775, a decrease of \$303,090 (55.8%) for the quarter ended March 31, 2010, as compared to the same period in 2009. This decrease in depletion expense was mainly due to the decrease in our oil and gas assets from our 2009 and 2008 impairments.

General and administrative expenses increased by \$37,263 or 4.1%, from \$903,782 for the quarter ended March 31, 2009, to \$941,045 for the period in 2010. This was primarily due to a credit recorded in 2009 pertaining to our outside consulting costs. Marketing expense for the quarter ended March 31, 2010, decreased \$61,955, or 29.1%, to \$150,752, compared to \$212,707 for the period in 2009. Marketing expense varies from period to period according to the number of marketing events attended by personnel and their associated costs.

Legal and accounting expense decreased to \$191,997 for the period, compared to \$366,511 for period in 2009, a \$174,514 or 47.6% decrease. The decrease in legal and accounting expense was a result of higher legal fees in 2009 primarily related to the Pioneer litigation and the acquisition of Royale's new credit facility with Texas Capital Bank.

Interest expense decreased to \$5,509 for the quarter ended March 31, 2010, from \$18,961 for the same period in 2009, a \$13,452, or 70.9% decrease. This was due to a decrease in the usage of our bank line of credit and lower interest rate on funds borrowed. For the first quarters in 2010 and 2009, we had income tax benefits of \$219,989 and \$569,007, respectively, due to net operating losses in both periods.

Capital Resources and Liquidity

At March 31, 2010, Royale Energy had current assets totaling \$7,799,952 and current liabilities totaling \$10,128,359, a \$2,328,407 working capital deficit. We had cash and cash equivalents at March 31, 2010, of \$2,968,506 compared to \$3,835,282 at December 31, 2009.

In February 2009, we entered into a revolving credit agreement with Texas Capital Bank, N.A. secured by our oil and gas properties, of up to \$14,250,000. We also entered into a separate letter of credit facility with Texas Capital Bank of up to \$750,000, for the purposes of refinancing Royale's existing debt and to fund development, exploration and acquisition activities as well as other general corporate purposes. Under the terms of the agreement, Royale Energy may borrow, repay, and reborrow funds as necessary. At March 31, 2010, we had a current borrowing base and outstanding indebtedness on this loan of \$2,280,000.

At March 31, 2010, we were not in compliance with one financial covenant of our loan agreement with the bank, but we have obtained a waiver from the terms of that loan covenant. We are not in default on any principal, interest or sinking fund payment.

At March 31, 2010, our accounts receivable totaled \$2,255,740, compared to \$2,493,108 at December 31, 2009, a \$237,368 (9.5%) decrease, primarily due to lower receivables of oil and natural gas revenues. At March 31, 2010, our accounts payable and accrued expenses totaled \$4,727,319, a decrease of \$401,668 or 7.8% from the accounts payable at December 31, 2009, of \$5,128,987, mainly due to paying down our accounts payable.

Ordinarily, we fund our operations and cash needs from our available credit and cash flows generated from operations. We believe that we have sufficient liquidity for the remainder of 2010 and do not foresee any liquidity demands that cannot be met from cash flow or financing activities.

Operating Activities. For the quarter ended March 31, 2010, cash used by operating activities totaled \$217,097 compared to cash used by operating activities of \$565,680 for the same period in 2009, a \$348,583 difference. This difference was due to decreases in accounts payables, accounts receivable, and prepaid expenses.

Investing Activities. Net cash used by investing activities, primarily in capital acquisitions of oil and gas properties, amounted to \$475,929 for the period in 2010, compared to \$198,950 used by investing activities for the same period in 2009, a \$276,979 or 139.2% increase in cash used. This increase capital acquisition was due to the timing of the wells drilled in 2009. The process to fund the necessary vendors working on the wells drilled in early January 2009 began in late December 2008, whereas the process to fund the one well drilling in the first quarter of 2010 began in the same quarter. The expense and costs for these wells in the first quarter of 2009 were recorded in the quarter, but the actual cash usage due to prepayments occurred in December 2008.

Financing Activities. For the three months ended March 31, 2010, cash used by financing activities was \$173,750 compared to cash provided by financing activity of \$2,478,207 for the same period in 2009. This difference was primarily due to entering into the new credit agreement with Texas Capital Bank, and drawing down less on our new credit line to fund continued drilling and corporate operations.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Our major market risk exposure relates to pricing of oil and gas production. The prices we receive for oil and gas are closely related to worldwide market prices for crude oil and local spot prices paid for natural gas production. Prices have been volatile for the last several years, and we expect that volatility to continue. Monthly average natural gas prices ranged from a low of \$4.58 per Mcf to a high of \$5.79 per Mcf for the first three months of 2010. We have not entered into any hedging or derivative agreements to limit our exposure to changes in oil and gas prices or interest rates.

Item 4. Controls and Procedures

As of March 31, 2010, an evaluation was performed under the supervision and with the participation of our management, including our CEO and CFO, of the effectiveness of the design and operation of our disclosure controls and procedures. These controls and procedures are based on the definition of disclosure controls and procedures in Rule 13a-15(e) and Rule 15d-15(e) promulgated under the Securities Exchange Act of 1934. Based on that evaluation, our management, including the CEO and CFO, concluded that our disclosure controls and procedures were effective as of March 31, 2010.

No changes occurred in our internal control over financial reporting during the three months ended March 31, 2010, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II OTHER INFORMATION

Item 1 Legal Proceedings

National Fuel Corporation (“NFC”) v. Royale Energy, Inc., No. 080800735, Uintah County, Utah. NFC filed the current lawsuit seeking to challenge a settlement agreement from a prior lawsuit over management of property in which Royale is the 75% owner and operator and NFC is a non-operator with a 25% ownership. On April 27, 2010, the court entered an order voiding the prior settlement agreement and establishing a new case scheduling order for litigation discovery. Royale intends to file an interlocutory appeal of the April 27 decision with the Utah Supreme Court.

Item 1A Risk Factors

Please review the risk factors contained in our Annual Report on Form 10-K for the year ended December 31, 2009.

Item 6 Exhibits

- 31.1 Rule 13a-14(a)/15d-14(a) Certification
- 31.2 Rule 13a-14(a)/15d-14(a) Certification
- 32.1 18 U.S.C. § 1350 Certification
- 32.2 18 U.S.C. § 1350 Certification

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.

ROYALE ENERGY, INC.

Date: August /s/ Donald H. Hosmer
4, 2010

Donald H. Hosmer, Co-President
and Co-Chief Executive Officer

Date: August /s/ Stephen M. Hosmer
4, 2010

Stephen M. Hosmer, Co-President,
Co-Chief Executive Officer, and
Chief Financial Officer

