

Citadel Exploration, Inc.  
Form 10-Q  
August 19, 2011

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

**Form 10-Q**

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

**For the quarterly period ended June 30, 2011**

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

**Commission file number 333-164850**

**CITADEL EXPLORATION, INC.**

(Exact name of registrant as specified in its charter)

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(State or other jurisdiction of  
incorporation or organization)

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

**420 Bryant Circle, Unit D  
Ojai, California 93023**

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(Address of principal executive offices)

**(530) 871-1484**

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(Registrant's telephone number, including area code)

*Copies of Communications to:*

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San Diego, CA 92101  
(619) 704-1310  
Fax (619) 704-0556

Indicate by check mark whether the issuer (1) 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 by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T

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(§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes  No

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

Large accelerated filer

Accelerated filer

Non-accelerated filer  (Do not check if a smaller reporting company) Smaller reporting company

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

Yes  No

The number of shares of Common Stock, \$0.001 par value, outstanding on August 3, 2011 was 20,220,000 shares.

**CITADEL EXPLORATION, INC.**  
**QUARTERLY PERIOD ENDED JUNE 30, 2011**

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**Item 1. Financial Statements.**

**CITADEL EXPLORATION, INC.**  
**(FORMERLY SUBPRIME ADVANTAGE, INC.)**  
**(A DEVELOPMENT STAGE COMPANY)**  
**CONSOLIDATED BALANCE SHEETS**

|   | June 30,<br>2011<br>(unaudited) | December 31,<br>2010<br>(audited) |
|---|---------------------------------|-----------------------------------|
| <b>ASSETS</b>   |                                 |                                   |
| Current assets:   |                                 |                                   |
| Cash  | \$ 119                          | \$ -                              |
| Prepaid Expenses  | 10,330                          | -                                 |
| Total current assets  | 10,449                          | -                                 |
| Oil and gas properties  | 137,773                         | 81,323                            |
| Website, net  | 1,337                           | -                                 |
| Total assets  | \$ 149,559                      | \$ 81,323                         |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>   |                                 |                                   |
| Current liabilities:  |                                 |                                   |
| Accounts payable  | \$ 58,692                       | \$ 800                            |
| Accrued interest payable - related party  | 351                             | -                                 |
| Total current liabilities   | 59,043                          | 800                               |
| Long term liabilities:  |                                 |                                   |
| Notes payable - related party   | 81,200                          | -                                 |
| Total long term liabilities   | 81,200                          | -                                 |
| Total liabilities   | 140,243                         | 800                               |
| Stockholders' equity:   |                                 |                                   |
| Common stock, \$0.001 par value, 100,000,000 shares<br>authorized, 20,200,000 and 14,000,000 shares issued and outstanding<br>as of June 30, 2011 and December 31, 2010, respectively | 20,220                          | 14,000                            |
| Additional paid-in capital  | 80,569                          | 72,293                            |
| Stock payable   | 34,000                          | -                                 |
| Deficit accumulated during development stage  | (125,473)                       | (5,770)                           |
| Total stockholders' equity  | 9,316                           | 80,523                            |
| Total liabilities and stockholders' equity  | \$ 149,559                      | \$ 81,323                         |

See Accompanying Notes to Consolidated Financial Statements.

**(FORMERLY SUBPRIME ADVANTAGE, INC.)**  
**(A DEVELOPMENT STAGE COMPANY)**  
**CONSOLIDATED STATEMENT OF OPERATIONS**  
**(unaudited)**

|   | For the three months<br>ended |                  | For the six months<br>ended |                  |
|---|-------------------------------|------------------|-----------------------------|------------------|
|   | June 30,<br>2011              | June 30,<br>2010 | June 30,<br>2011            | June 30,<br>2010 |
| Revenue   | \$ -                          | \$ -             | \$ -                        | \$ -             |
| Operating expenses:   |                               |                  |                             |                  |
| General and administrative                                      | 6,324                         | -                | 7,717                       |                  |
| Amortization  | 38                            | -                | 38                          |                  |
| Professional fees   | 111,597                       | -                | 111,597                     |                  |
| Total operating expenses  | 117,959                       | -                | 119,352                     |                  |
| Other expenses:   |                               |                  |                             |                  |
| Interest expense - related party                                | (351)                         | -                | (351)                       |                  |
| Total other expenses  | (351)                         | -                | (351)                       |                  |
| Loss before provision for income taxes                          | (118,310)                     | -                | (119,703)                   |                  |
| Provision for income taxes                                      | -                             |                  | -                           |                  |
| Net loss  | \$ (118,310)                  | \$ -             | \$ (119,703)                | \$ -             |
| Weighted average number of common shares<br>outstanding - basic | 20,214,237                    | 14,000,000       | 16,025,635                  | 14,000,000       |
| Net loss per share - basic                                      | \$ (0.01)                     | \$ -             | \$ (0.01)                   | \$ -             |

**See Accompanying Notes to Consolidated Financial Statements.**







**CITADEL EXPLORATION, INC.**  
**(FORMERLY SUBPRIME ADVANTAGE, INC.)**  
**(A DEVELOPMENT STAGE COMPANY)**  
**CONSOLIDATED STATEMENT OF CASH FLOWS**  
**(unaudited)**

|  | For the six months<br>ended<br>June 30, |      | (Inception)<br>November 6, 2006<br>to<br>June 30,<br>2011 |
|--|---|------|---|
|  | 2011                                    | 2010 | 2011  |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES</b>                                    |   |      |   |
| Net loss   | \$ (119,703)                            | \$ - | \$ (125,473)  |
| Adjustments to reconcile net loss<br>to net cash used in operating activities: |   |      |   |
| Amortization   | 38                                      | -    | 38  |
| Changes in operating assets and liabilities:                                   |   |      |   |
| Increase in accounts payable   | 28,627                                  | -    | 29,427  |
| Increase in accrued interest payable - related party                           | 351                                     | -    | 351   |
| Net cash used in operating activities  | (90,687)                                | -    | (95,657)  |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES</b>                                    |   |      |   |
| Purchase oil and gas properties  | (66,780)                                | -    | (148,103)   |
| Website  | (1,375)                                 | -    | (1,375)   |
| Net cash used in investing activities  | (68,155)                                | -    | (149,478)   |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES</b>                                    |   |      |   |
| Proceeds from sale of common stock, net of offering costs                      | 77,761                                  | -    | 164,054   |
| Proceeds from notes payable - related party                                    | 81,200                                  | -    | 81,200  |
| Net cash provided by financing activities                                      | 158,961                                 | -    | 245,254   |
| NET CHANGE IN CASH   | 119                                     | -    | 119   |
| CASH AT BEGINNING OF YEAR  | -                                       | -    | -   |
| CASH AT END OF YEAR  | \$ 119                                  | \$ - | \$ 119  |
| <b>SUPPLEMENTAL INFORMATION:</b>   |   |      |   |
| Interest paid  | \$ -                                    | \$ - | \$ -  |
| Income taxes paid  | \$ -                                    | \$ - | \$ -  |

**See Accompanying Notes to Consolidated Financial Statements.**



## **NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

### Basis of presentation

The condensed interim financial statements included herein, presented in accordance with United States generally accepted accounting principles and stated in US dollars, have been prepared by the Company, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations, although the Company believes that the disclosures are adequate to make the information presented not misleading.

These statements reflect all adjustments, consisting of normal recurring adjustments, which in the opinion of management, are necessary for fair presentation of the information contained therein. It is suggested that these condensed interim financial statements be read in conjunction with the financial statements of the Company for the year ended December 31, 2010 and notes thereto included in the Company's 10-K annual report and all amendments. The Company follows the same accounting policies in the preparation of interim reports.

Results of operations for the interim period are not indicative of annual results.

### Principles of Consolidation

For the year ended December 31, 2010, the consolidated financial statements include the accounts of Citadel Exploration, LLC. For the six months ended June 30, 2011, the consolidated financial statements include the accounts of Citadel Exploration, Inc. and Citadel Exploration, LLC. All significant intercompany balances and transactions have been eliminated. Citadel Exploration, Inc. and Citadel Exploration, LLC will herein be collectively referred to as the Company.

### Nature of operations

Currently, the Company is focused on the acquisition and development of oil and gas resources in California. The Company has not yet found oil and gas resources in commercially exploitable quantities and is engaged in exploring land in an effort to discover them. The Company has been in the exploration stage since its formation and has not realized any revenues from its planned principal operations.

### Use of estimates

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

**NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

Stock-based compensation

The Company records stock based compensation in accordance with the guidance in ASC Topic 718 which requires the Company to recognize expense related to the fair value of its employee stock option awards. This eliminates accounting for share-based compensation transactions using the intrinsic value and requires instead that such transactions be accounted for using a fair-value-based method. The Company recognizes the cost of all share-based awards on a graded vesting basis over the vesting period of the award.

Earnings per share

The Company follows ASC Topic 260 to account for the earnings per share. Basic earnings per common share ( EPS ) calculations are determined by dividing net income by the weighted average number of shares of common stock outstanding during the year. Diluted earnings per common share calculations are determined by dividing net income by the weighted average number of common shares and dilutive common share equivalents outstanding. During periods when common stock equivalents, if any, are anti-dilutive they are not considered in the computation.

Oil and gas properties

The Company uses the full cost method of accounting for its oil and natural gas properties. Under this method, all acquisition, exploration, development and estimated abandonment costs incurred for the purpose of acquiring and finding oil and natural gas are capitalized within cost centers. At December 31, 2010 and 2009, the Company had one cost center California. Unevaluated property costs are excluded from the amortization base until determination of the existence of proved reserves on the respective property or until the requirement for impairment. Unevaluated properties are reviewed at the end of each quarter to determine whether portions of the costs should be reclassified to the full cost pool and thereby subject to amortization. Sales of oil and natural gas properties are accounted for as adjustments to the net full cost pool with no gain or loss recognized, unless the adjustment would significantly alter the relationship between capitalized costs and proved reserves.

Capitalized costs of oil and natural gas properties evaluated as having, or not having, proved reserves are amortized in the aggregate by country using the unit-of-production method based upon estimated proved oil and natural gas reserves. For amortization purposes, relative volumes of oil and natural gas production and reserves are converted at the energy equivalent conversion rate of six thousand cubic feet of natural gas to one barrel of crude oil. Amortizable costs include estimates of future development costs of proved undeveloped reserves. The costs of properties not yet evaluated are not amortized until evaluation of the property. Such evaluations for a well and associated lease rights are made when it is determined whether or not the well has proved oil and natural gas reserves. Other unevaluated

properties are evaluated for impairment as of the end of each calendar quarter based upon various factors at the time, including drilling plans, drilling activity, management's estimated fair values of lease rights by project, and remaining lives of leases.

**NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

Capitalized costs of oil and natural gas properties (net of related deferred income taxes) may not exceed a ceiling amount equal to the present value, discounted at 10% per annum, of the estimated future net cash flows from proved oil and natural gas reserves plus the cost of unevaluated properties (adjusted for related income tax effects). Should capitalized costs exceed this ceiling amount, the excess is charged to earnings as an impairment expense, net of its related reduction of the deferred income tax provision. The present value of estimated future net cash flows is computed by applying the twelve-month historical averages of prices of oil and natural gas to estimated future production of proved oil and natural gas reserves as of period-end, less estimated future expenditures (at period-end rates) to be incurred in developing and producing the proved reserves and assuming continuation of economic conditions existing at period-end. The present value of future net cash flows of proved reserves excludes future cash outflows associated with settling asset retirement obligations that have been accrued on the balance sheet.

Revenue recognition

The Company recognizes oil and natural gas revenues from our interests in producing wells when production is delivered to, and title has transferred to, the purchaser and to the extent the selling price is reasonably determinable. Gas-balancing arrangements are accounted for using the sales method.

Recent pronouncements

The Company has evaluated the recent accounting pronouncements through ASU 2011-07 and believes that none of them will have a material effect on the company's financial statements.

**NOTE 2 GOING CONCERN**

The accompanying financial statements have been prepared assuming that the Company will continue as a going concern, which contemplates the recoverability of assets and the satisfaction of liabilities in the normal course of business. As noted above, the Company is in the development stage and, accordingly, has not yet generated revenues from operations. Since its inception, the Company has been engaged substantially in financing activities and developing its business plan and incurring start up costs and expenses. As a result, the Company incurred accumulated net losses from Inception (November 6, 2006) through the period ended June 30, 2011 of (\$125,473). In addition, the Company's development activities since inception have been financially sustained through debt and equity financing.

The ability of the Company to continue as a going concern is dependent upon its ability to raise additional capital from the sale of common stock and, ultimately, the achievement of significant operating revenues. These financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts, or amounts and classification of liabilities that might result from this uncertainty.



**NOTE 3 OIL AND GAS PROPERTIES**

The costs capitalized in oil and gas properties as of June 30, 2011 and December 31, 2010 are as follows:

|                            | <u>2011</u> | <u>2010</u> |
|----------------------------|-------------|-------------|
| Oil and gas property lease | \$ 51,653   | \$ 41,323   |
| Exploration                | 86,120      | 40,000      |
|                            | \$ 137,773  | \$ 81,323   |

On January 31, 2009, the Company entered into an oil, gas and mineral lease with an unrelated third party. The Company has the right to develop and operate the leased premises for an initial term of three years and the lease will continue as long as the Company continues actual drilling operations and continued development. The initial minimum lease payment of \$20,661 was made upon execution of the lease and the two remaining minimum lease payments of \$20,661 were due on January 31, 2010 and 2011. Additionally, the Company is obligated to pay royalties to the unrelated third party. On oil and gas from all wells on the leased premises, the royalty is a total of 20% of the market value. The royalty payments are due on or before the last day of each month for the preceding month's activity. If the royalty payment is not made timely, the Company will owe a 10% per annum interest on the royalties due.

**NOTE 4 NOTES PAYABLE RELATED PARTY**

Notes payable consists of the following at:

|   | June 30,<br>2011 | December<br>31,<br>2010 |
|---|------------------|-------------------------|
| Note payable to an entity owned and controlled by an officer, director and shareholder, unsecured, 4% interest, due upon demand | \$ 60,000        | \$ -                    |
| Note payable to an entity owned and controlled by an officer, director and shareholder, unsecured, 4% interest, due upon demand | 8,450            | -                       |

|   |        |      |
|---|--------|------|
| Note payable to an entity owned and controlled by an officer, director and shareholder, unsecured, 4% interest, due upon demand | 12,750 | -    |
|   | \$     |      |
|   | 81,200 | \$ - |

Interest expense for the six months ended June 30, 2011 and 2010 was \$351 and \$0, respectively. Interest expense for the three months ended June 30, 2011 and 2010 was \$351 and \$0, respectively.

**NOTE 5 STOCKHOLDERS EQUITY**

The Company is authorized to issue 100,000,000 shares of its \$0.001 par value common stock.

On March 2, 2011, the Company effected a 12-to-1 forward stock split of its \$0.001 par value common stock with a record date of March 22, 2011.

## **NOTE 5 STOCKHOLDERS EQUITY (CONTINUED)**

All shares and per share amounts have been retroactively restated to reflect the split discussed above.

On May 6, 2011, the Company issued 14,000,000 shares to an individual in exchange for a 100% interest in Citadel Exploration, LLC. As part of the Membership Purchase Agreement the former officers and directors agreed to cancel 7,696,000 shares of common stock. On May 3, 2011, the transaction was closed and 100% interest in Citadel Exploration, LLC was acquired by the Company. For accounting purposes, the acquisition of Citadel Exploration, LLC by the Company has been recorded as a reverse acquisition of a public company and recapitalization of Citadel Exploration, LLC based on the factors demonstrating that Citadel Exploration, LLC represents the accounting acquirer. The historic financial statements of Citadel Exploration, LLC and related entities, while historically presented as an LLC equity structure, have been retroactively presented as a corporation for comparability purposes. The Company changed its business direction and is now an oil and gas company.

On May 20, 2011, the Company sold 62,500 shares of common stock for cash of \$50,000. As of June 30, 2011, the Company issued 20,000 shares of common stock. The remaining 42,500 shares have not been issued and has been recorded to stock payable.

During the six months ended June 30, 2011, there have been no other issuances of common stock.

## **NOTE 6 WARRANTS AND OPTIONS**

As of June 30, 2011, there were no warrants or options outstanding to acquire any additional shares of common stock.

## **NOTE 7 MATERIAL AGREEMENTS**

On May 3, 2011, the Registrant, completed a Membership Purchase Agreement and Plan of Reorganization originally dated February 28, 2011, (the Original Agreement ) with Citadel Explorations, LLC, a California Limited Liability Company ( Citadel LLC ) acquiring 100% of Citadel, LLC 's outstanding membership interest in exchange for 14,000,000 shares of common stock, concurrent with the Closing. Additionally, the Original Agreement sets forth

conditions that the Company shall have obtained a cancellation of 7,696,000 shares of common stock. The Original Agreement with Citadel, LLC, provides the Company with the ownership of 100% of Citadel, LLC, which is involved in the oil and gas operating business.

Additionally, the officers and board of directors of the Company will resign and appoint Armen Nahabedian, to serve as Chief Executive Officer, President, Secretary, Treasurer, and a Director of the Registrant. Mr. Nahabedian shall serve as a Director of the Registrant until the next annual meeting of stockholders, or until successors have been elected.

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

This Quarterly Report on Form 10-Q contains forward-looking statements and involves risks and uncertainties that could materially affect expected results of operations, liquidity, cash flows, and business prospects. These statements include, among other things, statements regarding:

- o  
our ability to diversify our operations;
- o  
exploration risks such as drilling unsuccessful wells;
- o  
our ability to attract key personnel;
- o  
our ability to operate profitably;
- o  
our ability to efficiently and effectively finance our operations, and/or purchase orders;
- o  
inability to achieve future sales levels or other operating results;
- o  
inability to raise additional financing for working capital;
- o  
inability to efficiently manage our operations;
- o  
the inability of management to effectively implement our strategies and business plans;

o

the unavailability of funds for capital expenditures and/or general working capital;

o

the fact that our accounting policies and methods are fundamental to how we report our financial condition and results of operations, and they may require management to make estimates about matters that are inherently uncertain;

o

deterioration in general or regional economic conditions;

o

changes in U.S. GAAP or in the legal, regulatory and legislative environments in the markets in which we operate;

o

adverse state or federal legislation or regulation that increases the costs of compliance, or adverse findings by a regulator with respect to existing operations;

as well as other statements regarding our future operations, financial condition and prospects, and business strategies. These forward-looking statements are subject to certain risks and uncertainties that could cause our actual results to differ materially from those reflected in the forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those discussed in this Quarterly Report on Form 10-Q, and in particular, the risks discussed under the heading "Risk Factors" in Part II, Item 1A and those discussed in other documents we file with the Securities and Exchange Commission. We undertake no obligation to revise or publicly release the results of any revision to these forward-looking statements. Given these risks and uncertainties, readers are cautioned not to place undue reliance on such forward-looking statements.

*References in the following discussion and throughout this quarterly report to we , our , us , Citadel , the Company similar terms refer to Citadel Exploration, Inc. unless otherwise expressly stated or the context otherwise requires.*

## **OVERVIEW AND OUTLOOK**

### **Background**

Citadel Exploration, Inc., formerly Subprime Advantage, Inc., is a development stage company incorporated in the State of Nevada in December of 2009. On February 28, 2011, we entered into an agreement for the acquisition of 100% of the membership interest of Citadel Exploration, LLC ( CEL ), a California limited liability company.

On March 2, 2011, we changed our name from Subprime Advantage, Inc. to Citadel Explorations, Inc. in anticipation of the completion of the acquisition of 100% of all of the outstanding membership interest of CEL. The acquisition of 100% of the outstanding membership interest of CEL was completed on May 3, 2011. As a result of the completion of the acquisition, we are an oil and gas exploration company with operations in the Salinas Basin of California.

### **Recent Addition to Management**

On August 9, 2011, we appointed Mr. Armen Nahabedian as Chief Executive Officer, President and a Director of the Company. Prior to the appointment of Mr. Nahabedian, we accepted the resignation of Mr. Michael J. Finch as Chief Executive Officer and President but remained as a Director of the Company.

Mr. Nahabedian is a fourth generation oil and gas explorer in the state of California. In 1999, Mr. Nahabedian joined the United States Marine Corp as an infantryman and reached the rank of Corporal (E-4) before serving in operation Iraqi Freedom and receiving an honorable discharge in 2003. Mr. Nahabedian immediately thereafter went to work in the oil fields of the South San Joaquin Valley for his family's oil company, The Nahabedian Exploration Group. After early success in his exploration efforts Mr. Nahabedian became a regional supervisor and managed the drilling operations for some of the deepest exploratory wells drilled in the state of California from 2004 through 2007. In 2007, Mr. Nahabedian then joined The Nahabedian Exploration Group as a partner and supervised land acquisition efforts (over 750,000 acres leased or optioned) and prospect generation. Mr. Nahabedian continued to act as an operational supervisor and in 2009, he became involved in business development and finance. Acting as the company's primary fund raiser Mr. Nahabedian educated himself on public financing and securities and with the assistance of an experienced legal team formed Citadel Exploration Inc in 2011.

## **Our Operations**

As a result of completing the acquisition of the Shallow Indian Oil Development Project, located in the Bitterwater sub-basin of the Salinas Basin in California, consisting of 688.71 acres of leased property through the acquisition of 100% of the outstanding membership interest of CEL on May 3, 2011, our focus has been redirected to the oil and gas operations of CEL. We are now an oil and gas exploration, development and production company. Our principal strategy is to focus on the acquisition of oil and natural gas mineral leases that have existing production and cash flow. Once acquired, we strive to implement an accelerated development program utilizing capital resources, a regional operating focus, an experienced management and technical team, and enhanced recovery technologies to attempt to increase production and increase returns for our stockholders. Our oil and natural gas acquisition and development activities are currently focused in the Salinas Basin of California.



## **Going Concern**

The financial statements included in this filing have been prepared in conformity with generally accepted accounting principles that contemplate the continuance of the Company as a going concern, which contemplates the realization of assets and liquidation of liabilities in the normal course of business. However, the Company is in the development stage and, accordingly, has not generated revenues from operations. As shown on the accompanying financial statements, the Company has incurred a net loss of \$125,473 for the period from inception (November 6, 2006) to June 30, 2011. These conditions raise substantial doubt about the Company's ability to continue as a going concern.

The future of the Company is dependent upon its ability to obtain financing and upon future profitable operations from the development of its oil and gas business opportunities.

## **RESULTS OF OPERATIONS**

For accounting purposes, the acquisition of Citadel Exploration, LLC by the Company has been recorded as a reverse acquisition of a public company and recapitalization of Citadel Exploration, LLC based on the factors demonstrating that Citadel Exploration, LLC represents the accounting acquirer. The historic financial statements of Citadel Exploration, LLC and related entities, while historically presented as an LLC equity structure, have been retroactively presented as a corporation for comparability purposes.

Since our inception on November 6, 2006 through June 30, 2011, we have not generated any revenues.

Operating expenses totaled \$117,959 during the three months ended June 30, 2011 and \$119,352 during the six months ended June 30, 2011 as compared to \$0 in the prior year. Operating expenses primarily consisted of general and administrative fees and professional fees in the six and three months ended June 30, 2011.

General and administrative fees increased \$6,324 from the three months ended June 30, 2010 to the three months ended June 30, 2011. This increase was primarily as a result of having a license/permit expense in the period ended in 2011 and not in the same period a year ago.

General and administrative fees increased \$7,717 from the six months ended June 30, 2010 to the six months ended June 30, 2011. This increase was primarily as a result of having a license/permit expense in the period ended in 2011 and not in the same period a year ago.

Professional fees increased \$111,597 from the three and six months ended June 30, 2010 to the three and six months ended June 30, 2011. The increase was primarily due to an increase in legal fees.

### **Liquidity and Capital Resources**

As of June 30, 2011, we did not have any cash or cash equivalents. The following table provides detailed information about our net cash flow for all financial statement periods presented in this Quarterly Report. To date, we have financed our operations through the issuance of stock and borrowings.

The following table sets forth a summary of our cash flows for the six months ended June 30, 2011 and 2010:

|   | Six Months Ended |      |
|---|------------------|------|
|   | 2011             | 2010 |
| Net cash used in operating activities     | \$(90,687)       | -    |
| Net cash used in investing activities     | (68,155)         | -    |
| Net cash provided by financing activities | 158,961          | -    |
| Net increase in Cash                      | 119              | -    |
| Cash, beginning of year                   | -                | -    |
| Cash, end of year                         | \$119            | -    |

As of June 30, 2011, we continue to use traditional and/or debt financing to provide the capital we need to run the business.

On April 8, 2011, our wholly-owned subsidiary, Citadel Exploration, LLC, executed a \$50,000 line of credit with The Nahabedian Group ( TNG ), a related third party. During the quarter ended June 30, 2011, we received \$12,750 from TNG. The note is due on upon demand and bears interest at a rate of 4% per year.

On May 11, 2011, our wholly-owned subsidiary, Citadel Exploration, LLC, executed a \$50,000 line of credit with Gold or Glory, Inc. ( Gold or Glory ), a related third party. During the quarter ended June 30, 2011, we received \$8,450 from Gold or Glory. The note is due on upon demand and bears interest at a rate of 4% per year.

On May 31, 2011, our wholly-owned subsidiary, Citadel Exploration, LLC, executed a \$100,000 line of credit with Black Hawk Oil Company, LLC ( Black Hawk ), a related third party. During the quarter ended June 30, 2011, we received \$60,000 from Black Hawk. The note is due on upon demand and bears interest at a rate of 4% per year.

During the three and six months ended June 30, 2011 and June 30, 2010, we had interest expense of \$351 and \$0, respectively.

In May 2011, we received \$50,000 as a result of the private placement of 62,500 shares of our common stock at \$0.80 per share, pursuant to an exemption under the provisions of Regulation D-506 promulgated under the Securities Act of 1933.

Without cash flow from operations we will require additional cash resources, including the sale of equity or debt securities, to meet our planned capital expenditures and working capital requirements for the next 12 months. We will require additional cash resources due to changed business conditions, implementation of our strategy to successfully develop our Shallow Indian Oil Development Project, or acquisitions we may decide to pursue. If our own financial resources and then current cash-flows from operations are insufficient to satisfy our capital requirements, we may seek to sell additional equity or debt securities or obtain additional credit facilities. The sale of additional equity securities will result in dilution to our stockholders. The incurrence of indebtedness will result in increased debt service obligations and could require us to agree to operating and financial covenants that could restrict our operations or modify our plans to grow the business. Financing may not be available in amounts or on terms acceptable to us, if at all. Any failure by us to raise additional funds on terms favorable to us, or at all, will limit our ability to expand our business operations and could harm our overall business prospects.

Our ability to obtain additional capital through additional equity and/or debt financing, and Joint Venture or Working Interest partnerships will also be important to our expansion plans. In the event we experience any significant problems assimilating acquired assets into our operations or cannot obtain the necessary capital to pursue our strategic plan, we may have to reduce the growth of our operations. This may materially impact our ability to increase revenue and continue our growth.

### **Off-Balance Sheet Arrangements**

As of the date of this Current Report, we did not have any off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that is material to investors.

### **Operation Plan**

Our plan is to focus on the acquisition and drilling of prospective oil and natural gas mineral leases. Once we have tested a prospect as productive, subject to availability of capital, we will implement a development program with a regional operating focus in order to increase production and increase returns for our stockholders. Exploration, acquisition and development activities are currently focused in California. Depending on availability of capital, and other constraints, our goal is to increase stockholder value by finding and developing oil and natural gas reserves at costs that provide an attractive rate of return on our investments.

We expect to achieve these results by:

Investing capital in exploration and development drilling and in secondary and tertiary recovery of oil as well as natural gas;

Using the latest technologies available to the oil and natural gas industry in our operations;

Finding additional oil and natural gas reserves on the properties we acquire.

In addition to raising additional capital we plan to take on Joint Venture (JV) or Working Interest (WI) partners who may contribute to the capital costs of drilling and completion and then share in revenues derived from production. This economic strategy may allow us to utilize our own financial assets toward the growth of our leased acreage holdings, pursue the acquisition of strategic oil and gas producing properties or companies and generally expand our existing operations.

Because of our limited operating history we have yet to generate any revenues from the sale of oil or natural gas. Our activities have been limited to raising capital, negotiating WI agreements, becoming a publicly traded company and preliminary analysis of reserves and production capabilities from our exploratory test wells.

Our future financial results will depend primarily on: (i) the ability to continue to source and screen potential projects; (ii) the ability to discover commercial quantities of natural gas and oil; (iii) the market price for oil and natural gas; and (iv) the ability to fully implement our exploration and development program, which is dependent on the availability of capital resources. There can be no assurance that we will be successful in any of these respects, that the prices of oil and gas prevailing at the time of production will be at a level allowing for profitable production, or that we will be able to obtain additional funding to increase our currently limited capital resources.

### **Item 3. Quantitative and Qualitative Disclosure About Market Risk**

This item is not applicable as we are currently considered a smaller reporting company.

### **Item 4T. Controls and Procedures**

#### *Evaluation of Disclosure Controls and Procedures*

Our Chief Executive Officer, Armen Nahabedian, and our Principal Financial Officer, Christopher Whitcomb evaluated the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended) as of the end of the period covered by this Report. Based on that evaluation and assessment, Mr. Armen Nahabedian and Mr. Christopher Whitcomb concluded that our disclosure controls and procedures are designed at a reasonable assurance level and are effective to provide reasonable assurance that information we are required to disclose in the reports that we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our principal executive and principal financial officer, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

#### *Changes in Internal Control Over Financial Reporting*

There were no changes in our internal control over financial reporting that occurred during our most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

*Limitations on Effectiveness of Controls and Procedures*

In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives. In addition, the design of disclosure controls and procedures must reflect the fact that there are resource constraints and that management is required to apply its judgment in evaluating the benefits of possible controls and procedures relative to their costs.



## **PART II OTHER INFORMATION**

### **Item 1.**

#### **Legal Proceedings.**

From time to time, we may become involved in various lawsuits and legal proceedings which arise in the ordinary course of business. However, litigation is subject to inherent uncertainties, and an adverse result in these or other matters may arise from time to time that may harm our business. We are not presently a party to any material litigation, nor to the knowledge of management is any litigation threatened against us, which may materially affect us.

### **Item 1A. Risk Factors**

Our significant business risks are described in Item 1A. to Part II of Form 10-Q for the quarter ended March 31, 2011 and Item 1A. to Part I of Form 10-K for the year ended December 31, 2010 to which reference is made herein.

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

#### **Stock Issuances**

On May 6, 2011, we issued 14,000,000 shares of our restricted common stock to the managing member of Citadel Exploration, LLC in exchange for 100% of the membership interest of Citadel Exploration, LLC.

On May 20, 2011, we sold 62,500 shares of our restricted common stock to an accredited investor for a total purchase price of \$50,000 all which was paid in cash. Of the 62,500 shares, 20,000 shares have been issued and 42,500 shares are in the process of being issued.

We believe that the issuance and sale of the above shares was exempt from the registration and prospectus delivery requirements of the Securities Act of 1933 by virtue of Section 4(2) and Regulation D Rule 506. The shares were sold

directly by us and did not involve a public offering or general solicitation. The recipients of the shares were afforded an opportunity for effective access to files and records of the Company that contained the relevant information needed to make their investment decision, including the financial statements and 34 Act reports. We reasonably believed that the recipients, immediately prior to the sale of the shares, were accredited investors and had such knowledge and experience in our financial and business matters that they were capable of evaluating the merits and risks of their investment. The recipients had the opportunity to speak with our management on several occasions prior to their investment decision. There were no commissions paid on the issuance and sale of the shares.

### **Issuer Purchases of Equity Securities**

We did not repurchase any of our equity securities from the time of our inception on November 6, 2006 through the period ended June 30, 2011.

### **Item 3. Defaults Upon Senior Securities.**

None.

**Item 5. Other Information.**

On August 9, 2011, we appointed Mr. Armen Nahabedian as Chief Executive Officer, President and a Director of the Company. Prior to the appointment of Mr. Nahabedian, we accepted the resignation of Mr. Michael J. Finch as Chief Executive Officer and President but remained as a Director of the Company.

Mr. Nahabedian is a fourth generation oil and gas explorer in the state of California. In 1999, Mr. Nahabedian joined the United States Marine Corp as an infantryman and reached the rank of Corporal (E-4) before serving in operation Iraqi Freedom and receiving an honorable discharge in 2003. Mr. Nahabedian immediately thereafter went to work in the oil fields of the South San Joaquin Valley for his family's oil company, The Nahabedian Exploration Group. After early success in his exploration efforts Mr. Nahabedian became a regional supervisor and managed the drilling operations for some of the deepest exploratory wells drilled in the state of California from 2004 through 2007. In 2007 Mr. Nahabedian then joined The Nahabedian Exploration Group as a partner and supervised land acquisition efforts (over 750,000 acres leased or optioned) and prospect generation. Mr. Nahabedian continued to act as an operational supervisor and in 2009 he became involved in business development and finance.

**Item 6. Exhibits.**

| <b>Exhibit No.</b> | <b>Description</b>  |
|--------------------|---|
| 31.1               | Certification of Chief Executive Officer pursuant to Exchange Act Rules 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 |
| 31.2               | Certification of Chief Financial Officer pursuant to Exchange Act Rules 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 |
| 32.1               | Certifications of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002                    |
| 32.2               | Certifications of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002                    |
| 101.INS*           | XBRL Instance Document  |
| 101.SCH*           | XBRL Taxonomy Extension Schema  |

101.CAL\* XBRL Taxonomy Extension Calculation Linkbase

101.DEF\* XBRL Taxonomy Extension Definition Linkbase

101.LAB\* XBRL Taxonomy Extension Label Linkbase

101.PRE\* XBRL Taxonomy Extension Presentation Linkbase

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*XBRL (Extensible Business Reporting Language) information is furnished and not filed or a part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, is deemed not filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and otherwise is not subject to liability under these sections.*

**SIGNATURE**

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.

**CITADEL EXPLORATION, INC.**

Date: August 18, 2011

By:

/S/ Armen Nahabedian

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Armen Nahabedian  
Chief Executive Officer  
(Principal Executive Officer and duly authorized signatory)