

TRI VALLEY CORP
Form 10-Q
November 10, 2008

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2008

Commission File No. 001-31852

Tri-Valley Corporation
(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of incorporation or organization)

84-0617433
(I.R.S. Employer Identification No.)

4550 California Avenue, Suite 600, Bakersfield, California 93309
(Address of principal executive offices)

(661) 864-0500
(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 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 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 | <input type="checkbox"/> | Accelerated filer | <input checked="" type="checkbox"/> |
| Non-accelerated filer | <input type="checkbox"/> | Smaller reporting company | <input type="checkbox"/> |

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 Registrant's common stock outstanding at October 31, 2008 was 27,370,367.

TRI-VALLEY CORPORATION

INDEX

| | Page |
|--|-----------|
| PART I - <u>FINANCIAL INFORMATION</u> | 3 |
| Item 1. <u>Consolidated Financial Statements</u> | 3 |
| Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u> | 14 |
| Item 3. <u>Quantitative and Qualitative Disclosures about Market Risk</u> | 20 |
| Item 4. <u>Controls and Procedures</u> | 20 |
| PART II - <u>OTHER INFORMATION</u> | 20 |
| Item 1A. <u>Risk Factors</u> | 20 |
| Item 2. <u>Unregistered Sales of Equity Securities</u> | 21 |
| Item 6. <u>Exhibits</u> | 21 |
| <u>SIGNATURES</u> | 21 |

Table of Contents

PART I

FINANCIAL INFORMATION

Item 1. Unaudited Consolidated Financial Statements

TRI-VALLEY CORPORATION
CONSOLIDATED BALANCE SHEETS

ASSETS

| | September 30, 2008 (Unaudited) | December 31, 2007 (Audited) |
|--|--------------------------------------|-----------------------------------|
| Current assets | | |
| Cash | \$ 644,043 | \$ 3,955,610 |
| Cash restricted to OPUS I use | 8,455,928 | 3,712,083 |
| Accounts receivable, trade | 2,910,986 | 313,521 |
| Prepaid expenses | 12,029 | 12,029 |
| Total current assets | 12,022,986 | 7,993,243 |
| Property and equipment, net | | |
| Proved properties | 2,204,746 | 2,143,907 |
| Unproved properties | 4,509,568 | 2,414,843 |
| Rigs | 1,458,258 | 6,731,758 |
| Other property and equipment | 6,047,102 | 4,942,145 |
| Total property and equipment, net | 14,219,674 | 16,232,653 |
| Other assets | | |
| Deposits | 159,833 | 338,772 |
| Invest in marketable securities (Note 4) | 101,052 | 440,000 |
| Investments in partnerships | 17,400 | 17,400 |
| Goodwill | 212,414 | 212,414 |
| Other | 20,413 | 20,413 |
| Total other assets | 511,112 | 1,028,999 |
| Total assets | \$ 26,753,772 | \$ 25,254,895 |

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

Table of Contents

LIABILITIES AND STOCKHOLDERS' EQUITY

| | September 30, 2008 (Unaudited) | December 31, 2007 (Audited) |
|--|--------------------------------------|-----------------------------------|
| Current liabilities | | |
| Notes payable | \$ 388,396 | \$ 402,003 |
| Accounts payable and accrued expenses | 4,048,326 | 5,699,153 |
| Deferred revenue | 328,524 | 242,163 |
| Amounts payable to joint venture participants | 2,123,375 | 281,419 |
| Advances from joint venture participants, net | 642,390 | 3,671,927 |
| Total current liabilities | 7,531,011 | 10,296,665 |
| Non-Current Liabilities | | |
| Asset retirement obligation | 282,395 | 240,394 |
| Long-term portion of notes payable | 1,910,429 | 2,355,707 |
| Total non-current liabilities | 2,192,824 | 2,596,101 |
| Total liabilities | 9,723,835 | 12,892,766 |
| Minority interest | 2,745,524 | 249,945 |
| Stockholders' equity | | |
| Common stock, \$.001 par value; 100,000,000 shares authorized; 27,368,367 and 25,077,184 issued and outstanding at September 30, 2008, and December 31, 2007, respectively | 27,368 | 25,077 |
| Less: common stock in treasury, at cost, 100,025 shares | (13,370) | (13,370) |
| Capital in excess of par value | 45,161,398 | 37,090,714 |
| Additional paid in capital – warrants | 710,599 | 782,729 |
| Additional paid in capital - stock options | 2,449,920 | 1,800,642 |
| Accumulated deficit | (33,805,498) | (27,586,553) |
| Accumulated other comprehensive income | (246,004) | 12,945 |
| Total stockholders' equity | 14,453,116 | 12,112,184 |
| Total liabilities, minority interest and stockholder's equity | \$ 26,753,772 | \$ 25,254,895 |

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

Table of Contents

TRI-VALLEY CORPORATION
CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

| | For the Three Months Ended September 30, | | For the Nine Months Ended September 30, | |
|--|---|--------------------|--|--------------------|
| | 2008 | 2007 | 2008 | 2007 |
| Revenues | | | | |
| Sale of oil and gas | \$ 1,195,022 | \$ 204,699 | 2,823,396 | \$ 536,900 |
| Gain on sale of asset | 1,154 | - | 662,376 | - |
| Rig income | - | 266,404 | 1,122,384 | 2,077,273 |
| Drilling & Development | - | 3,285,227 | - | 3,285,227 |
| Other income | 227,528 | 156,260 | 727,805 | 829,200 |
| Interest income | 1,752 | 61,776 | 30,530 | 262,083 |
| Total Revenues | 1,425,456 | 3,974,366 | 5,366,491 | 6,990,683 |
| Costs and expenses | | | | |
| Oil and gas lease expense | 189,487 | 56,352 | 566,519 | 260,845 |
| Mining exploration expenses | 93,012 | 61,058 | 223,383 | 174,210 |
| Drilling and development | - | 1,890,199 | - | 2,748,288 |
| Rig operations | 219,194 | 179,896 | 1,098,775 | 959,904 |
| Depletion, depreciation and amortization | 196,860 | 253,745 | 911,230 | 740,062 |
| Interest | 31,327 | 69,555 | 185,529 | 218,221 |
| Impairment loss (Note 8) | - | 229,569 | 315,328 | 476,431 |
| General and administrative | 2,122,482 | 2,560,953 | 8,349,245 | 7,789,171 |
| Total costs and expenses | 2,852,362 | 5,301,327 | 11,650,009 | 13,367,132 |
| Loss before minority interest | (1,426,906) | (1,326,961) | (6,283,518) | (6,376,449) |
| Minority interest | (229,507) | - | (233,276) | - |
| Net Loss | (1,197,399) | (1,326,961) | (6,050,242) | (6,376,449) |
| Basic net loss per share: | | | | |
| Loss from operations | \$ (.04) | \$ (.05) | \$ (.22) | \$ (.26) |
| Basic loss per common share | \$ (.04) | \$ (.05) | \$ (.22) | \$ (.26) |
| Weighted average number of shares outstanding | 27,278,817 | 24,667,768 | 27,189,267 | 24,692,750 |
| Potentially dilutive shares outstanding | 30,245,662 | 28,039,242 | 30,288,830 | 28,061,268 |

No dilution is reported since net income is a loss per SFAS 128

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

Table of Contents

TRI-VALLEY CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

| | For the Nine Months Ended September 30, | |
|---|--|----------------|
| | 2008 | 2007 |
| Cash Flows from Operating Activities | | |
| Net loss | \$ (6,050,242) | \$ (6,376,449) |
| Adjustments to reconcile net income to net cash used from operating activities: | | |
| Depreciation, depletion and amortization | 911,230 | 740,062 |
| Loss on Impairment of Fixed Assets | 315,328 | 476,431 |
| Minority interest | (233,276) | - |
| Stock options | 577,064 | 688,564 |
| Gain on sale of property | (662,376) | - |
| Warrants | - | 316,852 |
| Changes in operating capital: | | |
| Increase in prepaids | - | (509,239) |
| Decrease in deposits and other assets | 178,939 | 150,000 |
| Increase in accounts receivable | (2,597,465) | 44,106 |
| Decrease in accounts payable, deferred revenue and accrued expenses | (1,564,466) | 1,887,506 |
| Increase accounts payable to joint venture participants and related parties | 1,841,956 | (100,469) |
| Decrease in advances from joint venture participants | (3,029,537) | 912,319 |
| Net Cash Used by Operating Activities | (10,312,845) | (1,770,317) |
| Cash Flows from Investing Activities: | | |
| Proceeds from sale of property | 7,388,654 | - |
| Proceeds from the sale of marketable securities | 79,999 | - |
| Investment in marketable securities | - | (380,000) |
| Buy back of minority interest in GVPS | (418,648) | (3,285,126) |
| Capital expenditures | (5,897,856) | (3,669,191) |
| Net Cash Provided / (Used) by Investing Activities | 1,152,149 | (7,334,317) |
| Cash Flows from Financing Activities | | |
| Principal payments on long-term debt | (458,885) | (314,409) |
| Net proceeds from additional paid in capital – stock options | 293,514 | 358,548 |
| Net proceeds from additional paid in capital – warrants | - | 658,400 |
| Net proceeds from minority interest holders – Great Valley Drilling/Great Valley Production | 2,978,800 | - |
| Stock issuance costs | (1,314,711) | (649,900) |
| Net proceeds from issuance of common stock | 9,094,256 | 5,966,831 |
| Net Cash Provided by Financing Activities | \$ 10,592,974 | \$ 6,019,470 |

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

Table of Contents

TRI-VALLEY CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
FOR THE NINE MONTHS ENDED
September 30, 2008 and 2007
(Unaudited)

NOTE 1 - DESCRIPTION OF BUSINESS AND BASIS OF PRESENTATION

Description of Business

Tri-Valley Corporation (“TVC” or the Company), a Delaware corporation formed in 1971, is in the business of exploring, acquiring and developing petroleum and metal and mineral properties and interests therein.

The Company identifies reportable segments by product. The Company includes revenues from both external customers and revenues from transactions with other operating segments in its measure of segment profit or loss. The Company also includes interest revenue, DD&A, and other operating expenses in its measure of segment profit or loss. The results of these four segments are presented in Note 7 to the Consolidated Financial Statements.

The Company’s four industry segments are:

- Oil and gas operations include our share of revenues from oil and gas wells on which Tri-Valley Oil and Gas Company serves as operator, royalty income and production revenue from other partnerships in which we have operating or non-operating interests. It also includes revenues for consulting services for oil and gas related activities.
- Rigs and refurbishing operations began in 2006, when the Company acquired drilling rigs and began operating them through subsidiaries Great Valley Production Services, LLC, and Great Valley Drilling Company, LLC. Rig operations include income from rental of oil field equipment and income received from refurbishing and selling oilfield equipment.
- Minerals include the Company’s mining and mineral prospects and operations, and expenses associated with those operations.
- Drilling and development includes revenues received from oil and gas drilling and development operations performed for joint venture partners, including the Opus-I drilling partnership.

The Company has five subsidiaries:

- Tri-Valley Oil & Gas Company (“TVOG”) operates the oil & gas activities. TVOG derives the majority of its revenue from oil and gas drilling and turnkey development. TVOG primarily generates its own exploration prospects from its internal database, and also screens prospects from other geologists and companies. TVOG generates these geological “plays” within a certain geographic area of mutual interest. The prospect is then presented to potential co-ventures. The company deals with both accredited individual investors and energy industry companies. TVOG serves as the operator of these co-ventures. TVOG operates both the oil and gas production segment and the drilling and development segment of our business lines.
- Select Resources Corporation (“Select”) was created in late 2004 to manage, grow and operate the minerals segment of our business lines.

- Great Valley Production Services, LLC, (“GVPS”) was formed in 2006 to operate oil production services, well work over and drilling rigs, primarily for TVOG. In July of 2008, the drilling rigs were sold so that going forward the primary operations of GVPS will be to refurbish oilfield equipment for use in the

Table of Contents

NOTE 1 - DESCRIPTION OF BUSINESS AND BASIS OF PRESENTATION (continued)

Company's operations and for sale to outside third parties. During the third quarter Tri-Valley sold 21% of the ownership interest to private parties and has retained a 79% ownership interest in this subsidiary.

- Great Valley Drilling Company, LLC ("GVDC") was formed in 2006 to operate oil drilling rigs, primarily in Nevada where Tri-Valley has 17,000 acres of prospective oil leases. However, because rig availability is scarce in Nevada, GVDC has an opportunity to do contract drilling for third parties in both petroleum and geothermal projects. For the time being GVDC, whose operation began in the first quarter of 2007, expects its primary activity will be contract drilling for third parties. GVDC is 100% owned by TVC.

- Tri-Valley Power Corporation is inactive at the present time.

Basis of Presentation

The financial information included herein is unaudited; however, such information reflects all adjustments (consisting solely of normal recurring adjustments), which are, in the opinion of management, necessary for a fair statement of results for the interim periods. The results of operations for the nine month period ended September 30, 2008, are not necessarily indicative of the results to be expected for the full year.

The accompanying consolidated financial statements do not include footnotes and certain financial presentations normally required under generally accepted accounting principles in the United States of America; and, therefore, should be read in conjunction with our Annual Report on Form 10-K, filed with the Securities and Exchange Commission on March 14, 2008, for the year ended December 31, 2007.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company, its wholly owned subsidiaries, TVOG, Select, GVDC, Tri-Valley Power Corporation, since their inception. GVPS, where the Company has retained a 79% ownership interest is also included in the consolidation. Other partnerships in which the Company has an operating or nonoperating interest in which the Company is not the primary beneficiary and owns less than 51%, are proportionately combined. This includes Opus I, Martins-Severin, Martins-Severin Deep, and Tri-Valley Exploration 1971-1 partnerships. All material intra and intercompany accounts and transactions have been eliminated in combination and consolidation.

NOTE 2 - PER SHARE COMPUTATIONS

Per share computations are based upon the weighted-average number of common shares outstanding during each year. Common stock equivalents are not included in the computations since their effect would be anti-dilutive.

NOTE 3 – SUMMARY OF RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

Accounting for Business Combinations

During December 2007, the FASB issued SFAS No. 141 (R), "Business Combinations" ("SFAS No. 141(R)"), which establishes new accounting and disclosure requirements for recognition and measurement of identifiable assets, liabilities and goodwill acquired and requires that the fair value estimates of contingencies acquired or assumed be

considered as part of the original purchase price allocation. SFAS No. 141(R) is effective for periods beginning on or after December 15, 2008. This standard does not presently affect the Company's financial statements.

Table of Contents

NOTE 3 – SUMMARY OF RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS (continued)

Fair Value Measurements

In September 2006, the FASB issued SFAS No. 157, “Fair Value Measurements.” This Statement replaces multiple existing definitions of fair value with a single definition, establishes a consistent framework for measuring fair value and expands financial statement disclosures regarding fair value measurements. This Statement applies only to fair value measurements that already are required or permitted by other accounting standards and does not require any new fair value measurements. SFAS No. 157 is effective for fiscal years beginning subsequent to November 15, 2007. We adopted this Statement in the first quarter of 2008, and the adoption did not have a material impact on our financial position or results of operations.

The Fair Value Option for Financial Assets and Financial Liabilities

In February 2007, the FASB issued SFAS No. 159, “The Fair Value Option for Financial Assets and Financial Liabilities,” which permits an entity to measure certain financial assets and financial liabilities at fair value. The objective of SFAS No. 159 is to improve financial reporting by allowing entities to mitigate volatility in reported earnings caused by the measurement of related assets and liabilities using different attributes, without having to apply complex hedge accounting provisions. Under SFAS No. 159, entities that elect the fair value option (by instrument) will report unrealized gains and losses in earnings at each subsequent reporting date. The fair value option election is irrevocable, unless a new election date occurs. SFAS No. 159 establishes presentation and disclosure requirements to help financial statement users understand the effect of the entity’s election on its earnings, but does not eliminate disclosure requirements of other accounting standards. Assets and liabilities that are measured at fair value must be displayed on the face of the balance sheet. The Company adopted this statement effective beginning January 1, 2008, and the adoption did not have a material impact on our financial position or results of operations.

Noncontrolling Interest in Consolidated Financial Statements

In December 2007, the FASB issued SFAS No. 160, “Noncontrolling Interests in Consolidated Financial Statements — An Amendment of ARB No. 51”. SFAS No. 160 establishes new accounting and reporting standards for a noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. Specifically, this statement requires the recognition of a noncontrolling interest (minority interest) as equity in the consolidated financial statements. The amount of net income attributable to a noncontrolling interest will be included in consolidated net income on the face of the income statement. SFAS No. 160 requires that changes in a parent’s ownership interest in a subsidiary that do not result in deconsolidation are equity transactions if the parent retains its controlling financial interest. In addition, this statement requires that a parent recognize a gain or loss when a subsidiary is deconsolidated. Such gain or loss will be measured using the fair value of the noncontrolling equity investment on the deconsolidation date. SFAS No. 160 also includes expanded disclosures regarding the interests of the parent and its noncontrolling interest. SFAS No. 160 will be effective for the Company on January 1, 2009. We do not expect the adoption of SFAS No. 160 to have a material impact on our financial position or results of operations.

The Hierarchy of Generally Accepted Accounting Principles

In May 2008, the FASB issued SFAS No. 162, “The Hierarchy of Generally Accepted Accounting Principles”. SFAS No. 162 identifies the sources of accounting principles and the framework for selecting the principles used in the preparation of financial statements of nongovernmental entities that are presented in conformity with generally accepted accounting principles in the United States. The new standard becomes effective 60 days following the SEC’s approval of the Public Company Accounting Oversight Board amendments to AU Section 411. SFAS No. 162 is not expected to have a material impact on our consolidated financial position or results of operations.

Table of Contents

NOTE 4 – INVESTMENT

In the second quarter of 2007, the Company received 150,000 stock options for Duluth Metals common stock for providing executive and geological services for Duluth Metals. The stock options are exercisable at \$0.30 Canadian. During the fourth quarter of 2007, the options were exercised and converted into stock at a cost of \$47,055. During the second quarter of 2008, 30,000 shares of stock were sold at an average price of \$2.82 Canadian. The market value of each share of stock on September 30, 2008, was \$0.82 Canadian. The Company follows the provisions of Statement of Financial Accounting Standards No. 115 (SFAS 115), “Accounting for Certain Investments in Debt and Equity Securities.” SFAS 115 requires companies to classify their investments as trading, available-for-sale or held-to-maturity. The Company’s securities consist of stock which has been classified as available-for-sale. These are recorded in the financial statements at fair market value and any unrealized gains (losses) will be reported as a component of shareholder equity. At September 30, 2008, the cost basis net of write-downs, unrealized gains, unrealized losses and fair market value of the Company's holdings are as follows:

| | September 30, 2008 |
|----------------------|--------------------------|
| Net cost of equities | \$ 341,644 |
| Unrealized Losses | (240,592) |
| Fair Market Value | \$ 101,052 |

SFAS 115 requires that for each individual security classified as available-for-sale, a company shall determine whether a decline in fair value below the cost basis is other than temporary. If the decline in fair value is judged as such, the cost basis of the individual security shall be written down to fair value as a new cost basis and the amount of the write-down shall be reflected in other comprehensive income of the equity section. At September 30, 2008, the company's marketable securities had a fair market value of \$101,052. The unrealized loss of \$201,448 for the third quarter of 2008 is reported as other comprehensive income bringing the net unrealized loss inception to date to \$240,592.

This investment was translated into U.S. Dollars in accordance with SFAS No. 52, “Foreign Currency Translation.” The investment was translated at the rate of exchange on the balance sheet date.

NOTE 5 - CHANGES IN SECURITIES

Common Stock

During the third quarter of 2008, the Company issued 426,603 shares of common stock. Two employees exercised employee stock options during the quarter to purchase 9,500 shares totaling \$27,400. 417,103 shares were issued in private placements at prices of \$5.00 to \$7.49 per share, for a total consideration of \$ 2,420,688. Total stock issuance cost for the third quarter was \$374,826.

NOTE 6 – STOCK BASED COMPENSATION EXPENSE

Stock Based Compensation

Compensation expense charged against income for stock based awards in the third quarter of 2008 and 2007 was \$255,127 and \$35,354, pre-tax, respectively, and is included in general and administrative expense in the Consolidated Statement of Operations.

Table of Contents

NOTE 6 – STOCK BASED COMPENSATION EXPENSE (continued)

For further information regarding stock based compensation, please refer to Note 5 of the Notes to the Consolidated Financial Statements in the Annual Report on Form 10-K for the year ended December 31, 2007.

NOTE 7 - FINANCIAL INFORMATION RELATING TO INDUSTRY SEGMENTS

The Company reports operating segments according to SFAS No. 131, “Disclosure about Segments of an Enterprise and Related Information.”

The Company identifies four principal industry segments by products and services, which are described in Note 1 – Description of Business and Basis of Presentation – Description of Business. The Company includes revenues from both external customers and revenues from transactions with other operating segments in its measure of segment profit or loss.

The following table sets forth our revenues by segment for the nine months ended September 30, 2008 and the nine months ended September 30, 2007, in thousands:

| | Three Months Ended September 30 | | Nine Months Ended September 30 | |
|---------------------------------------|------------------------------------|----------|-----------------------------------|----------|
| | 2008 | 2007 | 2008 | 2007 |
| Sales and Other Revenues | | | | |
| Oil & Gas | \$ 1,425 | \$ 300 | 3,345 | \$ 894 |
| Rigs & refurbishing operations | - | 269 | 1,877 | 2,213 |
| Minerals | - | 120 | 144 | 598 |
| Drilling and Development | - | 3,285 | - | 3,286 |
| Consolidated Sales and Other Revenues | \$ 1,425 | \$ 3,974 | \$ 5,366 | \$ 6,991 |

The following table sets forth our operating income (loss) by segment, in thousands:

| | Three Months Ended September 30 | | Nine Months Ended September 30 | |
|--------------------------------|------------------------------------|------------|-----------------------------------|------------|
| | 2008 | 2007 | 2008 | 2007 |
| Operating income (loss) | | | | |
| Oil & Gas | \$ (644) | \$ (1,474) | \$ (3,940) | \$ (4,581) |
| Rigs & refurbishing operations | (73) | (984) | (921) | (1,083) |
| Minerals | (194) | (159) | (363) | (310) |
| Drilling and Development | - | 1,395 | - | 537 |
| Non Segmented | (286) | (105) | (826) | (939) |
| Total income | (1,197) | (1,327) | (6,050) | (6,376) |

The following table summarizes our total assets, in thousands:

| | September 30, 2008 | December 31, 2007 |
|--------------|-----------------------|----------------------|
| Total Assets | | |
| Oil & Gas | \$ 22,970 | \$ 18,191 |

Edgar Filing: TRI VALLEY CORP - Form 10-Q

| | | |
|--------------------------------|-----------|-----------|
| Rigs & refurbishing operations | 1,903 | 4,703 |
| Minerals | 1,881 | 2,361 |
| Consolidated Total Assets | \$ 26,754 | \$ 25,255 |

12

Table of Contents

NOTE 8 – SALE OF RIG ASSETS & IMPAIRMENT

In June 2008, GVPS entered into an agreement to sell rigs and rig related equipment to Excalibur Well Services Corporation. During the 2nd quarter, the company recorded an impairment loss of \$315,328. The sale of the rigs and rig related equipment was completed during the third quarter and no gain or loss was recorded related to this sale due to the 2nd quarter impairment loss.

Property sold consisted of the following:

| | Original Carrying Amount | Impairment | Adjusted Carrying Value |
|------------------------|--------------------------------|--------------|-------------------------------|
| Drilling Rigs | \$ 4,441,850 | \$ (278,804) | \$ 4,163,046 |
| Drilling Rig Equipment | 560,746 | (30,410) | 530,336 |
| Vehicles | 112,732 | (6,114) | 106,618 |
| Total | \$ 5,115,328 | \$ (315,328) | \$ 4,800,000 |

Outstanding liabilities at June 30, 2008 related to these assets totaled \$364,124. Outstanding liabilities at September 30, 2008 related to these assets totaled \$0.

Table of Contents

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

Notice Regarding Forward-Looking Statements

This report contains forward-looking statements. The words, "anticipate," "believe," "expect," "plan," "intend," "estimate," "project," "could," "may," "foresee," and similar expressions are intended to identify forward-looking statements. These statements include information regarding expected development of Tri-Valley's business, lending activities, relationship with customers, and development in the oil and gas industry. Should one or more of these risks or uncertainties occur, or should underlying assumptions prove incorrect, actual results may vary materially and adversely from those anticipated, believed, estimated or otherwise indicated.

Results of Operations

Three months ended September 30, 2008 Compared to three months ended September 30, 2007

For the quarter ended September 30, 2008, revenue was \$1.4 million, compared to \$4.0 million in the third quarter of 2007, a decrease of \$2.6 million. We had an operating loss of about \$1.2 million in the third quarter of 2008, compared to a loss of \$1.3 million in the third quarter of 2007.

Revenues

The Company identifies reportable segments by products and services. The Company includes revenues from both external customers and revenues from transactions with other operating segments in its measure of segment profit or loss. The Company also allocates interest revenue and expense, DD&A, and other operating expenses in its measure of segment profit or loss. The following table sets forth our revenues by segment for the third quarter of 2008 and 2007, in thousands.

| | Three Months Ended September 30 | | Increase/ (Decrease) | Percentage Change (%) |
|-------------------------------|------------------------------------|----------|-------------------------|--------------------------|
| | 2008 | 2007 | | |
| Oil and gas | \$ 1,425 | \$ 300 | \$ 1,125 | 375 |
| Rig & refurbishing operations | - | 269 | (267) | (100) |
| Minerals | - | 120 | (120) | (100) |
| Drilling & development | - | 3,285 | (3,285) | (100) |
| Total revenues | \$ 1,425 | \$ 3,974 | \$ (2,549) | (64) |

Oil and gas revenues in the third quarter of 2008 included approximately \$1.4 million from the sale of oil and gas, compared to \$300 thousand in the third quarter of 2007. This also represents a quarter-over-quarter increase of 375%. The increase resulted from both significantly increased oil and gas production and increased commodity pricing.

The primary oil and gas activities during the third quarter of 2008 represented an ongoing rapid build-up of operations per our "Operation Catapult" initiative which is focused on rapidly accelerating production of oil and gas and resultant operating cash flow, and investment returns to our Partners and Shareholders. In summary, key activity included the completion of Phase I drilling for the TVOG Opus I Drilling Program LP, progressive cyclic steaming of heavy oil wells, ongoing conversion of temporary to permanent facilities, installation of a fuel gas line and test headers, a variety of remedial work on existing wellbores, additional new perforated zones on existing wells, additional field-level staffing to handle our uplift, and continued, prudent progression of the existing asset exploitation programs.

The Company expects that the oil and gas production will continue to grow increasing revenues and that the operating income of this segment will be improved by year-end 2008.

Table of Contents

Operating Income (Loss)

The following table sets forth our operating income (loss) by segment in the second quarter of 2008 and 2007, in thousands.

| | Three Months | | Increase/ (Decrease) | Percentage Change (%) |
|-------------------------------|----------------------------|------------|-------------------------|--------------------------|
| | Ended September 30 2008 | 2007 | | |
| Total operating income | | | | |
| Oil & Gas | \$ (644) | \$ (1,474) | 830 | 56 |
| Rig & refurbishing operations | (73) | (984) | 911 | 93 |
| Minerals | (194) | (159) | (35) | (22) |
| Drilling and Development | - | 1,395 | (1,395) | (100) |
| Non-segmented | (286) | (105) | (181) | (172) |
| Total income | \$ (1,197) | \$ (1,327) | \$ 130 | 10 |

Income for the quarter ended September 30, 2008 was a loss of \$1.2 million, compared to \$1.3 million loss in the third quarter of 2007, a decrease in the loss of \$0.1 million.

Nine months ended September 30, 2008 Compared to nine months ended September 30, 2007

For the nine months ended September 30, 2008, revenue was \$5.3 million, compared to \$7.0 million in the first nine months of 2007, a decrease of \$1.7 million. We had an operating loss of about \$6.0 million in the first nine months of 2008, compared to a loss of \$6.4 million in the first nine months of 2007.

General and administrative expenses were \$8.3 million for the first nine months ended September 30, 2008, compared to \$7.7 million for the first nine months of 2007, an increase of \$0.6 million. \$0.4 million of this increase was due to non-recurring expenses associated with the buy back of the minority interest of GVPS. The remaining \$0.2 million increase was due to the addition of new staff.

Revenues

The Company identifies reportable segments by products and services. The Company includes revenues from both external customers and revenues from transactions with other operating segments in its measure of segment profit or loss. The Company also allocates interest revenue and expense, DD&A, and other operating expenses in its measure of segment profit or loss. The following table sets forth our revenues by segment for the first nine months of 2008 and 2007, in thousands.

| | Nine Months | | Increase/ (Decrease) | Percentage Change (%) |
|-------------------------------|----------------------------|----------|-------------------------|--------------------------|
| | Ended September 30 2008 | 2007 | | |
| Oil and gas | \$ 3,345 | \$ 894 | \$ 2,451 | 274 |
| Rig & refurbishing operations | 1,877 | 2,213 | (336) | (15) |
| Minerals | 144 | 598 | (454) | (76) |
| Drilling & development | | 3,286 | (3,286) | (100) |
| Total revenues | \$ 5,366 | \$ 6,991 | \$ (1,625) | (23) |

Table of Contents

Operating Income (Loss)

The following table sets forth our operating income (loss) by segment for the first nine months of 2008 and 2007, in thousands.

| | Nine Months | | Increase/ (Decrease) | Percentage Change (%) |
|-------------------------------|----------------------------|------------|-------------------------|--------------------------|
| | Ended September 30 2008 | 2007 | | |
| Total operating income | | | | |
| Oil & Gas | \$ (3,940) | \$ (4,581) | 641 | 14 |
| Rig & refurbishing operations | (921) | (1,083) | 162 | 15 |
| Minerals | (363) | (310) | (53) | (17) |
| Drilling and Development | - | 1,395 | (1,395) | (100) |
| Non-segmented | (826) | (939) | 113 | 12 |
| Total operating income | \$ (6,050) | \$ (6,376) | \$ 326 | 5 |

Income for the nine months ended September 30, 2008 was a loss of \$6.0 million, compared to \$6.3 million loss in the first nine months of 2007, a decrease in the loss of \$0.3 million.

Oil and Gas

Work continued apace on facilities build up of the Company's primary development property in the Oxnard, California oilfields to support increase of production. Recovery of the heavy oil from the Upper Vaca Tar Sand formation requires drilling of wells with horizontal bores in the range of 1,200 – 1,500 feet, specialized completion techniques, extensive high pressure/high temperature steaming, addition of light gravity oil diluent, water separation and shipping by truck to a pipeline terminal. The steam generators are now supplied by natural gas, and an oil sales pipeline is being arranged.

Tri-Valley is presently steaming and producing from seven horizontal well bores and evaluating various zones on its Hunsucker Lease. It recently added the Lenox Ranch across the street with 20 idle vertical wells that are being systematically re-worked in preparation for steaming and production. New horizontal wells are planned for drilling in the fourth quarter since horizontal bores can produce at rates greater than what vertical wells can do.

On Tri-Valley's Moffat Ranch gas field west of Madera, California, the new 48-X well continues to be produced at a choked back rate to avoid sand/water build-up. At the Company's Temblor properties in the South Belridge and Edison oil fields, modest oil production continues as the pilot water flood project build up continues and new shallow wells are contemplated for the fourth quarter 2008 and first quarter 2009.

Tri-Valley is raising the last \$15 million of the \$100 million TVOG Opus I Drilling Program LP, primarily to attain some 20 horizontal wells at the Oxnard properties. When these well bores have continuous steam from injector wells, the Company believes sustained production in the 10,000 barrels of oil can be obtained according to a report by the late Canadian steam assisted gravity drainage of heavy oil expert, Dr. Ralph Butler. Other drilling programs, both exploratory and development are being considered for launch in 2009.

Rig & refurbishing operations

There were no revenues from rig operations in the third quarter compared to \$0.27 million in the third quarter of 2007. GVPS did not realize operating revenue in the third quarter of 2008 due to the sale of rig assets in July. The operating loss in the third quarter of 2008 was \$73 thousand, compared to an operating loss of \$0.9 million in the third quarter of 2007, or a decrease in the loss of \$0.8 million.

Table of Contents

In June 2008, GVPS agreed to sell all of its production and drilling rigs and down hole tools to Excalibur Well Services, Inc. in exchange for cash and a highly attractive, preferred client status for well servicing. The sale was completed in July 2008 for a price of \$4.8 million. GVPS recognized an impairment loss of \$0.3 million in the second quarter to write down the value of the assets being sold to the sales price. GVPS retained its fleet of 17 steam generators.

GVDC drilled one petroleum well in Nevada for another operator during the second quarter. The rig is presently idle and is looking for its next jobs. More than 120 petroleum and geothermal wells have been staked or permitted for future drilling in Nevada. We believe that GVDC's experience in Nevada provides a profitable opportunity for the business line in 2008 and beyond, and the Company has stepped up its marketing activity in Nevada, Idaho and eastern Washington. With engine modifications to accommodate stricter air quality rules, the rig can also operate in California.

Minerals Activities

There were no revenues from minerals activities in the third quarter of 2008 compared to \$120 thousand in the third quarter of 2007, due to a decrease in consulting revenue. With the primary emphasis of the Company to boost oil and gas production, the properties of Select Resources largely have been in a care and maintenance status. However, Jim Bush, formerly Vice President of exploration for Tri-Valley Oil and Gas Co. and now President of Select Resources, has assumed the charge of activating and monetizing the properties through finding joint venture partners, spin-off or outright sale.

For the third quarter, mineral programs continued the assessment and compilation of geologic information as was done in the previous quarter for the Calder, Richardson, and Shorty Creek properties in Alaska, but made significant advances in understanding the Admiral Calder calcium carbonate deposit (see below). Select also continued to pursue candidates for management and officer levels in the company and consultants to assist in property development. Select continues to be devoted to returning the Admiral Calder mine to a profitable undertaking, continues to explore precious metal opportunities, continues to include uranium as a new commodity of interest, and has reduced efforts directed towards acquiring new base metals and industrial minerals properties. More specific information is provided in the following sections.

Industrial Minerals

During the third quarter, Select continued low-cost monitoring and security at the Admiral Calder calcium carbonate quarry in Alaska and undertook additional maintenance activity and equipment testing. Several sections of the crushing and material handling plant were operated as were various parts of the maintenance shop and the on-site analytical lab. As a result, we now have a much better grasp of what needs to be done prior to directing any effort towards restart and it is not overwhelming.

In addition to the above, Select made significant advances in understanding the Admiral Calder calcium carbonate deposit itself. This deposit is almost certainly in the top 10% of the globe's deposits and by some experts is considered to be in the top 1%. We believe it may well be one of the top 5 or 10 calcium carbonate deposits in the world. The chemical purity and high whiteness/brightness characteristics make the product suitable for high-end uses as in adhesives, plastics, rubber, paint products, paper, and possibly in high end paper applications (although we are currently investigating its characteristics when pulverized to the sub 10 micron size-range). Even more important, it appears as though the amount of the high quality product in the deposit is easily twice the estimates originally provided and perhaps triple or more. These findings significantly change the overall life and potential production rates of the operation, and along with that the potential profit. In short, our compilation of many different reports and reworking of the calculations of the in-ground resource are indicating that this deposit is much better than we had

originally envisioned, and along with that so are the economics. To further enhance the value of these findings, the third quarter saw the beginning of inquiries about developing the property and meetings with potential joint venture partners. In addition to the ground calcium carbonate (GCC) market and chemical grade calcium carbonate market, Select is further evaluating the site's potential to produce new product types that can competitively participate in new (i.e. first-time for Calder) market categories. These include dimension stone, and ways to minimize and exploit mine waste (such as using low grade material for acid rock drainage control at other mines). Putting the quarry into a revenue-generating status remains a Select priority. In parallel with the above, Select is considering candidates for a long-term position to head up the development of this property.

Table of Contents

Select continues to maintain a number of industrial mineral projects in six western states in a hold status, pending further review. Commodities in these projects include barite, sand & gravel, aggregate, limestone, dolomite, calcium carbonate, cinder, and other industrial mineral commodities.

Precious Metals

Select continues to solicit mining interests for the larger scale exploration on both the Richardson and Shorty Creek properties, as well as identifying a field site manager for both properties. Select has contacted, and continues to solicit, candidates for these positions.

Shorty Creek has been described by the State Geologist of Alaska as perhaps the best un-drilled gold exploration project in Alaska. It should be pointed out that Select's neighbor, International Tower Hill, located only a few miles northerly from Shorty Creek, has delineated in excess of 3 million in-the-ground ounces of gold via drilling.

The Richardson District is arguably the most prospective gold exploration district in Alaska and it remains under-explored. Tri-Valley has found native gold at 60 locations along a 20 mile swath suggesting the possibility of a large system.

Uranium

Select has begun soliciting and reviewing uranium opportunities in a very targeted and selective manner. Select is adhering rigorously to strict high-end criteria for these properties.

Base Metals

Base Metals operations continue to be on hold.

Non-segmented items

The non-segmented items consist of stock option expense and interest expense. Non-segmented items decreased from \$0.9 million in the first nine months of 2007, to \$0.8 million in the first nine months of 2008. Stock option expense for the first nine months of 2008 was \$0.6 million, compared to \$0.7 million for the first nine months of 2007, a decrease of \$0.1 million. Interest expense for the first nine months of 2008 was \$0.2 million, unchanged from the first nine months of 2007.

Capital Resources and Liquidity

In 2002 through the third quarter of 2008, our drilling activities have been largely funded by selling interests in our OPUS I drilling partnership. We do not borrow in order to fund drilling activities. Our continued drilling activity relies on our ability to raise money for projects through drilling partnerships or other joint ventures.

Current assets were about \$12.0 million at September 30, 2008, up from \$8.0 million at year end 2007, an increase of \$4.0 million. Cash on hand increased from \$7.6 million at year end 2007 compared to \$9.0 million at September 30, 2008. Trade accounts receivable increased to \$2.9 million at September 30, 2008, compared to \$0.3 million at year end 2007 due to increased oil and gas production. Current liabilities decreased to about \$7.5 million at September 30, 2008, compared to \$10.3 million at year end 2007.

Operating Activities

We had a negative cash flow of \$10.3 million for the nine months ended September 30, 2008 compared to a negative cash flow of \$1.7 million for the same period in 2007. The negative cash flow in the current period is due mainly to our loss from operations along with our decrease in advances from joint venture participants and an increase in accounts receivable. Our loss from operations was approximately \$6.0 million for the nine months ended September 30, 2008 compared to a \$6.3 million loss for the same period in 2007.

Table of Contents

Investing Activities

Net cash provided by investing activities was \$1.1 million for the first nine months of 2008 compared to \$7.3 million used for the first nine months of 2007. During 2008, the company received \$7.3 million from the sale of rig assets, three steam generators and a heater treater. \$5.9 million was used towards capital expenditures, primarily the drilling of new wells and we used \$0.4 million to buy back membership units in GVPS.

Financing Activities

Net cash provided by financing activities was \$10.6 million for the first nine months of 2008 compared to \$6.0 million for the same period of 2007. We received \$9.0 million from sales of restricted shares of common stock in privately negotiated transactions including the exercise of stock options by employees. We used \$459,000 to pay down principal on long-term debt. The company raised \$2.9 million from the sale of partnership units in GVP. We have not planned any private placement of equity securities for the remainder of 2008, but we may continue to receive funds from privately negotiated transactions. We do not have a targeted or budgeted amount of equity financing activities.

Liquidity

The recoverability of our oil and gas reserves depends on future events, including obtaining adequate financing for our exploration and development program, successfully completing our planned drilling program, and achieving a level of operating revenues that is sufficient to support our cost structure. At various times in our history, it has been necessary for us to raise additional capital through private placements of equity financing. When such a need has arisen, we have met it successfully. It is management's belief that we will continue to be able to meet our needs for additional capital as such needs arise in the future. We may need additional capital to pay for our share of costs relating to the drilling prospects and development of those that are successful, and to acquire additional oil and gas leases, drilling equipment and other assets. The total amount of our capital needs will be determined in part by the number of prospects generated within our exploration program and by the working interest that we retain in those prospects.

During the remainder of 2008, we expect to expend approximately \$7 million on drilling activities. Funds for the majority of these activities will be provided by sales of partnership interests in the Opus-I drilling partnership, which will still be raising funds for development purposes. Tri-Valley's portion is expected to be approximately \$1.5 million. Our ability to complete our planned drilling activities in 2008 depends on some factors beyond our control, such as availability of equipment and personnel. Our actual capital commitments for fiscal year 2008 are less than \$2 million, but to expend \$7 million we will require additional capital from the OPUS partnership or other outside parties.

During the remainder of 2008, we expect expenditures of approximately \$ 0.2 million on mining activities, including mining lease and exploration expenses.

Should we choose to make an acquisition of producing oil and gas properties, such an acquisition would likely require that some portion of the purchase price be paid in cash, and thus would create the need for additional capital. Additional capital could be obtained from a combination of funding sources. The potential funding sources include:

- Cash flow from operating activities,
- Borrowings from financial institutions (which we typically avoid),
- Debt offerings, which could increase our leverage and add to our need for cash to service such debt (which we typically avoid),

- Additional offerings of our equity securities, which would cause dilution of our common stock,
- Sales of portions of our working interest in the prospects within our exploration program, which would reduce future revenues from its exploration program,
 - Sale to an industry partner of a participation in our exploration program,
- Sale of all or a portion of our producing oil and gas properties, which would reduce future revenues.

Table of Contents

Our ability to raise additional capital will depend on the results of our operations and the status of various capital and industry markets at the time such additional capital is sought. Accordingly, there can be no assurances that capital will be available to us from any source or that, if available, it will be on terms acceptable to us. The Company has no off balance sheet arrangements.

New Accounting Pronouncements

See Note 3 to our unaudited consolidated financial statements.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Tri-Valley Corporation does not engage in hedging activities and does not use commodity futures or forward contracts in its cash management functions.

Item 4. Controls and Procedures

As of September 30, 2008, an evaluation was performed under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, 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 as of September 30, 2008, our management, including the CEO and CFO concluded that our disclosure controls and procedures were effective to ensure that the information required to be disclosed by us in the reports that we file or submit under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms.

Management, including our CEO and CFO, have concluded that our disclosure controls and procedures provide reasonable assurance that the controls and procedures will meet their desired control objectives. In designing and evaluating our control system, management recognized that any control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance of achieving the desired control objectives. Further, the design of a control system must reflect the fact that there are resource constraints, and management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any that may affect our operations have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake.

During the third quarter of 2008, there were no changes in the Company's internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II - OTHER INFORMATION

Item 1A. Risk Factors

There have been no material changes from the risk factors previously disclosed in our Annual Report on Form 10-K for the fiscal year ended December 31, 2007.

Table of Contents

Item 2. Unregistered Sales of Equity Securities

During the third quarter of 2008, the Company issued 426,603 shares of restricted common stock to 60 private investors at prices of \$5.00 to \$7.49 per share for a total consideration of \$2,420,688.

All of these transactions were conducted in reliance on the exemption from registration requirements of the Securities Act of 1933 contained in Section 4(2) of that Act.

Item 6. Exhibits

| Item | Description |
|-------------|--|
| <u>31.1</u> | Rule 13a-14(a)/15d-14(a) Certification |
| <u>31.2</u> | Rule 13a-14(a)/15d-14(a) Certification |
| <u>32.1</u> | 18 U.S.C. Section 1350 Certification |
| <u>32.2</u> | 18 U.S.C. Section 1350 Certification |

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.

TRI-VALLEY CORPORATION

November 10, 2008

/s/F. Lynn Blystone
F. Lynn Blystone
Chairman, President and CEO

November 10, 2008

/s/ Arthur M. Evans
Arthur M. Evans
Chief Financial Officer