Journal of Forensic and Investigative Accounting
Volume 14: Issue 3, Special Issue 2022

Business Combination v. Asset Acquisition: KPMG's Earnings Management and Subsequent Litigation Involving Miller Energy Resources

D. Larry Crumbley
*Steve Grossman**

After the 2008 market crash, a number of financial companies were acquired at large discounts from their book value. One example was the purchase of Lehman Brothers by Barclay, resulting in an approximately 2.26 British pound sterling purchase gain (sometimes called negative goodwill). Another example is the purchase of HBOS plc by Lloyds Banking Group in 2009, resulting in an 11 billion British pound sterling bargain purchase gain for Lloyd.[1]

Nonfinancial companies also have been involved in bargain purchase gains. One such company, discussed in this article, was Miller Energy Resources, Inc. (Miller) headquartered in Knoxville, Tennessee. In total, KPMG paid around $6.2 million for its failed audit of this one client. Forensic accountants may provide valuable litigation services in disputes involving accounting misstatements. These accountants must study many documents pertaining to damages caused by companies and auditors in possible issues of fraud.

A Recent Non-Financial Example

Miller was an independent exploration and production company in East Tennessee. Miller went public in 1996 and for a number of years its stock was traded in the over-the-counter bulletin board exchange. The company was a relative insignificant player in the petroleum industry with total assets just under $3 million at fiscal 2003-year end.

California based Pacific Energy Resources Ltd. was disposing of its assets in the Cook Inlet region of Alaska in a bankruptcy proceeding. The assets were on the market for a year and were in the process of being "abandoned," as there were significant costs to maintain the property. Miller ultimately won the bid with $2.25 million in cash along with the assumption of approximately $2 million of liabilities in 2009. Miller's management along with its then auditors Sherb and Company LLP (now defunct) determined that the purchase of the assets was an asset acquisition rather than a business combination. Miller's subsequent auditors (KPMG) encouraged the company to change its accounting treatment in 2011 to a business combination.

Sherb and Company LLP was based in New York City, and the SEC charged the CPA firm with failed audits during 2007–2011 of three Chinese-based audit clients. On November 6, 2013, the firm and four accountants were charged and fined by the SEC for improper professional conduct and expressing the wrong unqualified opinions on the three China-based clients during a period when the SEC was investigating reverse mergers.[2]

There are significant differences in the accounting treatment between business combinations and asset acquisitions (e.g., bargain purchase gain). On Miller's Form 10-Q filed on March 22, 2010, a Bargain Purchase Gain of $277,414,756 was shown.[3] As a result of Miller's acquisition and recognition of the Bargain Purchase Gain, its assets expanded almost fifty-fold, and its fixed assets and oil and gas property accounted for almost all assets under successful efforts. The SEC

---

[1] Will Kenton, What Is a Bargain Purchase? *Investopedia*, December 13, 2020.
[2] SEC, SEC Charges New York-Based Audit Firm and Four Accountants for Failures in Audits of China-Based Companies, 2013-238, November 7, 2013. See also C.L. Martin and C.J. Russo, Sherb and Company LLP: A Triple Play of Misconduct, *J. of Business Cases & Applications*, Vol. 19, January 2018; Brittany Lang and John McGown, Chinese Reverse Mergers: Accounting Fraud and Stock Price Collapse, *J. of Forensic and Investigative Accounting*, Vol. 5, Issue 2, July–December 2013, pp. 175–199.
[3] Miller Energy Resources, Inc., *Form 10-Q for period ended January 31, 2010*, Page 16, filed on Mar. 22, 2010, *https://www.sec.gov/Archives/edgar/data/785968/000116169710000242/form10-q.txt.*

*The authors are, respectively, Professor, Texas A&M University—Corpus Christi, and Associate Professor, Texas A&M University.

charged former officers of Miller, KPMG, and KPMG personnel for inflating the value of its assets.[4] There also is a class action shareholder lawsuit pending against the external auditors KPMG.[5]

Business Combination vs. Asset Acquisition: FAS No. 141R

In Statement of Financial Accounting Standards No. 141R, Business Combinations, which was issued in 2007, a business is defined as "… an integrated set of activities and assets that is capable of being conducted and managed for the purpose of providing a return in the form of dividends, lower costs, or other economic benefits directly to investors or other owners, members, or participants." A transaction or other event is a business combination only if the assets acquired and liabilities assumed constitute a business; otherwise, the transaction or other event should be accounted for as an asset acquisition.

Inputs and processes applied to the assets acquired are essential, but outputs are not necessary to the definition of a business. The question is whether the integrated set of assets and activities acquired is capable of being conducted and managed to produce outputs. Even if the acquiree is not producing outputs on its own or is not operating the set as a business, but the acquirer can integrate the assets and activities into its own business to produce the outputs, the transaction or other event is a business combination.

The three elements of a business are defined as follows in the Statement:

a. "Input: Any economic resource that creates, or has the ability to create, outputs when one or more processes are applied to it
b. Process: Any system, standard, protocol, convention, or rule that when applied to an input or inputs, creates, or has the ability to create outputs
c. Output: The result of inputs and processes applied to those inputs that provide or have the ability to provide a return directly to investors or other owners, members, or participants."

If these three elements are present, then the acquisition is a business combination.

A bargain purchase is defined in the Statement as "… a business combination in which the total acquisition-date fair value of the identifiable net assets acquired exceeds the fair value of the consideration transferred … and requires the acquirer to recognize that excess in earnings as a gain attributable to the acquirer." This would be a bargain purchase gain reported on the income statement.

This Statement does not apply to acquisitions that do not meet the definition of a business. Such transactions should be accounted for as an asset acquisition. The cost of the acquired assets is allocated to the individual assets based on their relative fair values.

Bargain Purchase Gains

If a company purchases the net assets of another company for less than the fair market value, a bargain gain occurs. Deloitte describes how a bargain purchase gain may occur:[6]

> Bargain purchases could result from what might be viewed as market imperfections, including situations in which the seller may not have had adequate time to market the business and thus did not subject the sale to a competitive bidding process, or in which the seller was compelled to sell, such as in a forced liquidation or distressed sale. However, because it is expected that a seller would not accept less than fair value for its business, and additional

---

[4] U.S. Securities and Exchange Commission, *Accounting and Auditing Enforcement Release No. 3731 Miller Energy Resources, Inc., et al., January 12, 2016,* https://www.sec.gov/litigation/admin/ 2016/33-10000.pdf, *January 12, 216,* 12, https://222.sec.gov/litigation/admin/2016/33-10002.
[5] *Lewis Cosby et al. v. KPMG, LLP,* 3:16-CV-121-TAV-DCP (E.D. Tenn. 2021). For additional details of this dispute, see D.L. Crumbley and J. Ma, Miller Energy Resources: Analysis of an Accounting Scandal and the Corresponding Audit Failure, *Oil, Gas & Energy Quarterly*, March 2020, pp. 329–342 and Y. Chen, K. Capriotti, and J. D'Aquila, Miller Energy Fraud and KPMG's Audit Failure, *J. of Forensic & Investigative Accounting,* Special Issue, Vol. 13, Issue 3, 2021, pp. 530–539.
[6] Deloitte, A Roadmap to Accounting for Business Combinations, November 2020, p. 12.

potential buyers also would emerge to take advantage of a potential bargain and thus increase the price, bargain purchases resulting from underpayments relative to fair value do not occur frequently.

The Miller transaction was covered by Statement of Financial Accounting Standards No. 141 R, which was effective on or after the beginning of the first annual reporting period on or after December 15, 2008. If the transaction is a business combination, any gain is recognized as a bargain purchase gain on the acquisition date and is immediately recognized as earnings. If the transaction is an asset acquisition, the bargain purchase gain is not recognized as earnings. Instead, any difference between the fair value of the assets acquired over cost is allocated to certain assets based on relative fair market values. The purpose of the remainder of this article is to determine if Miller's purchase were a business combination or an asset purchase under FASB and how a consultant could gather evidence to demonstrate the answer to this dispute.

Why the Miller Purchase Transaction Was an Asset Acquisition

Miller's Alaska asset purchase should have been treated as an asset acquisition rather than a business combination under SFAS No. 141R, based upon numerous factors.

1. The initial intent was to purchase some of the assets as demonstrated by the signing of the Purchase and Sales Agreement dated November 24, 2009. The term "Alaska Interest" is defined as "Abandoned Assets." A Definitive Purchase Agreement is generally used for a merger, acquisition, or divestiture (also known as a stock purchase agreement or definitive merger agreement).
2. Miller's Registration Statement for fiscal years 2009–2010 states "Acquisition of Alaskan Assets of Pacific Energy Resources" (not purchasing the business).
3. The footnote on the financial statements (April 30, 2010) called the transaction a purchase of assets. Same on Form 8-K (3-29-2010). "The resulting assets and liabilities were deemed not to have been a separate business for purposes of preparing pro forma financials." Same language was on the Form 8-K/A, 12/10/2009.
4. A SEC letter dated June 7, 2011, made these critical observations under the SFAS No.141R guidance:
    - In November 2009, certain assets of Pacific Energy were permitted by the bankruptcy court to be sold in pieces.
    - The Pacific Energy administration and accounting staff were largely dismantled by October 2009.
    - The Alaska oil and gas wells had ceased production by August 31, 2009, and had not been fully operational for months.
    - Several of the wells had become inoperable, as the well casings had collapsed and required rework.
    - Osprey offshore drilling platform ceased production in July 2009, was missing parts and was inoperative, and none of the oil wells supported by the offshore drilling platform could resume production without substantial investment. Sherb audit Form 10-K said it would take $35 million to get Ospery back into operation.
5. Form 8-K, December 10, 2009, states "Therefore, the resulting assets and liabilities were deemed not to have been a separate business for purposes of preparing pro forma financial results ..."
6. Carlton Vogt III, CPA, Sherb's lead audit partner, in his deposition (pp. 32 and 45) said oil was not flowing, things are frozen up; oil pipes are hidden; the pipes are just marked as oil wells: cannot just flip a switch and get product.
7. Paul Boyd, CFO of Miller, in his deposition (p. 19) agreed that "these assets were not operational for several months before the acquisition to the bankruptcy … nor were accounting records maintained by Pacific Energy Alaska." Records, of course, are important for inputs and processes.
8. Critical to the elements process/output was Miller's lack of experience as well as the Cook Inlet management teams' deficiencies.
    - Miller had no oil experience in Alaska.
    - Miller had no oil experience over water and/or deep wells.

- Miller's previous experience was small shallow wells in Eastern Tennessee near oil fields.
- The Cook Inlet management team were the same people that had failed the previous owners attempts to produce cash flow from their oil fields (output).

9. Cash flow and financing were needed to obtain any significant outputs:
   - The December 10, 2010, R. E. Davis Projection of Cash Flows for the Cook Inlet PV-10 Report Projected Cash Flow Requirements for Capital Investment of: Y/E 12-2010, $33,300,000; Y/E 12-2011, $55,600,000; Y/E 12-2012, $ 9,200,000; Y/E 12-2013, $23,675,000.
   - Miller did not have financing until May 2011 and funding only after KPMG audit report was released. Only $35,000,000 was available of the $115,000,000 needed. Guggenheim had all assets tied up.
   - SEC would not approve any S-3 equity funding by stock sales for two years for failure to include audited historical financials of the Alaska Operations. So, this important funding was not available.
   - Apparently, little or no capital was expended on the Alaska Assets for year-end April 30, 2010, and 2011.

10. David Hall, CEO of Miller's Alaska operation, overestimated the reserves by drastically underestimating expenses.

11. Using a pre-tax discount rate of 10 percent for all reserves (proved, probable, and possible) instead of an increasing rate, Miller simply added together the present value of the reserves and did not consider the confidence level of recovering the reserves.

12. An analysis of Cook Inlet Production versus Budget from April 30, 2010, through April 30, 2014, shows a shortfall of net oil of $298,249,146. So, Miller could not obtain necessary capital from its output.

13. Another complication was the fact that the Asset Retirement Obligation was probably greater than the total assets ($1,789,995 on March 22, 2010, Form 10-Q).

14. In the principal audit partner John Riordan's deposition (p. 40), he answered, "In general terms, yes, that's my understanding" to the question that Scott Boruff just went to the bankruptcy court and basically asked can I buy the assets if we bifurcate them …?" So, the assets were divided into good assets, bad assets, and sold.

15. Once KPMG took over the audit, Paul Boyd changed his mind when answering some SEC questions and called the purchase a business combination. He admitted that he received an email from audit partner John Riordan early in the morning to replace the language of asset acquisition with business combination—even though the phrase asset acquisition was in its previous Forms 10-K and 8-K.

16. This change was a change in an accounting method which should have caused a retroactive change in the two prior years of the financial statements as a correction of an error, a debit adjustment to retained earnings of $277 million (a prior period adjustment), shown net of income taxes. Paul Boyd later said in his deposition that he stood by what he said in the prior Forms 10-K and 8-K (p. 32). He also stated that he did not believe the prior Forms 10-K and 8-K were changed (p. 32).

A consultant or expert witness could present this evidence in a report or testimony in the courtroom for the plaintive after evaluating the available evidence on whether the Miller transaction was a business combination or asset acquisition. The defendant's fact or expert witness would have to try to overcome the evidence or explain it away.

KPMG's Audit and the SEC's Reaction[7]

In an email dated January 6, 2011, KPMG's Senior Manager Lynne A. Lamkin alerted John Riordan, the principal audit partner, to the fact that Miller's Form 10-Ks called the purchase as an asset acquisition before they became Miller's auditor. Based upon the above facts and opinions, KPMG should have determined that the purchase of assets was a true asset acquisition, and that no bargain purchase gain could be shown. With the high write-up of the reserves, KPMG should have considered Miller a high-risk client, and if it did not feel that appropriate audit procedures could reduce that risk

[7] This section is based on U.S. Securities and Exchange Commission, Accounting and Auditing Enforcement Releases 3778 (June 7, 2016), 3779 (June 7, 2016), and 3888 (August 15, 2017) regarding Miller Energy Resources.

probably not accepted the engagement. John Riordan and KPMG classified Miller as a medium risk, even though the new reserve purchase represented 95% of Miller's total assets, and assets increased 5,000% after the purchase.

The SEC charged John Riordan and KPMG with not exercising professional care and professional skepticism in collecting audit evidence and documenting work papers. The SEC also indicated that KPMG and Riordan did not undertake adequate procedures to assess the risks when accepting Miller as a client.

KPMG did not adequately consider Miller's purchase of the Alaska assets, its history as a very low-priced stock, the inexperience of its personnel, its financing challenges, and its stream of net losses. In addition, Riordan had limited experience in auditing oil and gas companies in Alaska and therefore made bad judgements in reviewing the work of the specialists and failed to review the bankruptcy records of Pacific Energy Resources.

KPMG relied on a third-party petroleum engineering firm and an insurance broker. KPMG's Economic Valuation Service relied on numbers provided by Miller's engineer consultant. Riordan was aware of an article in *The Street Sweeper* opining that Miller's valuation of the Alaska assets was overstated, but he did not take any action to examine the evidence presented.

There also should have been an adjustment for the double counting of the $110 million fixed assets (shown both in fixed asset and the reserve estimates). KPMG also should not have increased the value of the reserves, ranging from $469 million to $531 million for the Alaska assets. Instead, impairment of the reserves was in order. The SEC was extremely critical of Miller's and KPMG's overestimation of oil and gas reserves. In hindsight, the actual production figures for years ending April 30, 2010, through April 30, 2014, showed that only 966,649 net barrels were produced. This total number was taken from Miller Energy's Form 10-Ks.

See Appendix A for excerpts from a letter by the SEC's Division of Corporation Finance to Miller asking for information on numerous points.

Subsequent Events

Miller filed an amended 10-K report admitting that the July 29, 2011, filing was wrong, but the amended one is correct and received an unqualified opinion from KPMG. Miller's stock price rose almost 50 percent. Miller's wholly owned subsidiary, Cook Inlet Energy, was beginning to get ready to begin operations in early 2011.

Mallik-Fita wrote in January 2012, in *Seeking Alpha* that Miller was a stock in which it would be wise to invest. "Miller's breakthrough moment was its consummation of one of the savviest deals ever seen in the industry: the 2009 acquisition of the Alaska Cook Inlet assets … for merely $5 million …" In response to public statements by a group of dissident shareholders in December 2013, Miller said that the company had "a very strong record of creating shareholder value over the last seven years … and a great opportunity to continue to create significant value."

In an SEC release on August 16, 2015, the SEC charged Miller, its former chief financial officer (Paul Boyd) and its Chief Operating Officer (David Hall) for inflating the values of oil and gas properties and therefore violating the anti-fraud provisions of U.S. Securities laws. The SEC also sought to bar Paul W. Boyd and Carlton Vogt (the Sherb's partner in charge of Miller's previous 2010 audit) from public company accounting. Miller filed for bankruptcy in October 2015.

In 2017, the SEC ordered KPMG to return its earnings from Miller with interest, a total of about $5.2 million, and pay a civil penalty of`$1 million. Principal auditor John Riordan was fined $25,000.

In 2018, the SEC fined Boyd and Hall $125,000 each and ordered Miller to pay a $5 million civil money penalty. Also defrauded investors filed a lawsuit against KPMG. A judge in May 2021, sided with the plaintiffs, agreeing to a class certification, and denied KPMG's bid to throw the lawsuit out. The trial was expected to begin in February 2022, but KPMG agreed to pay a $35 million settlement with the investors in March 2022, and the Tennessee court approved the settlement in July 2022.

Earnings Management and Fraud

Accountants can be involved as consultants or expert witnesses in securities class action lawsuits either for the plaintiff or the defendant. The plaintiff prefers damages to be large and the defendant prefers damages to be minimal. The forensic accountants often consult or testify about damage calculations which involve accounting and finance concepts.

Class action lawsuits allow injured parties to join together to seek repayment as a group. Once a class action suit is filed, the federal court determines whether the complaint can move forward.[8]

The hired consultant or expert witness must search and review many documents before reaching a decision. A forensic accountant at a minimum often will review the entity's financial statements, Form 10-Ks, Form 8-Ks, letters, reports, tax returns, FASB standards, SEC and PCAOB pronouncements, emails, pleadings, depositions, experts' reports, tax and legal documents and many other appropriate items. For example, an expert could use the SEC material that is in Appendix A in their expert report and testimony. In most trials, various experts and consultants are hired on both sides to help the attorneys. They prepare reports, go through depositions, and may testify in the courtroom.

Bharat Sarath provides evidence of earnings management in a 2019 working paper dealing with FDIC-assisted and non-FDIC-assisted bank acquisitions. With respect to fair value estimates, Sarath found that bargain purchase gains using fair values reflected the underlying economic assets more accurately in FDIC-assisted transactions where indemnification arrangements are part of the acquisition. However, management is more likely to present an overly optimistic picture in non-FDIC business bargain purchase gains (i.e., like in Miller).[9]

Steven Lilien et al. found that bargain purchase gains, especially Level 3 fair value estimates of acquired intangible assets, have consistently been used to smooth earnings without creating long-term market gains in the non-financial industries. They suggest managers are using the valuation of intangibles to avoid unfavorable earnings even though the valuations are not credible to investors.[10]

Justin Mikulka, an investigative reporter, has frequently written about external auditors helping to facilitate fraud in the oil industry, especially with estimations of reserves. He indicates that "getting an apparently reputable third party to put their name on the financial reports is one way to hide the fraudulent dealing, while also offering deniability to those committing fraud."[11]

The *Wall Street Journal* in 2019 reported that "thousands of shale wells drilled in the past five years are pumping less oil than their owners forecasted to investors."[12] Three Texas A&M University authors published a paper for the Society of Petroleum Engineers concluding that "reserves overstatements have occurred on a number of occasions, and for a variety of reasons in the oil and gas industry."[13] With respect to fair value measurements, three authors indicate that "the convergence of recent events in regulations and standards setting is placing an increasing difficulty and perhaps in some cases unrealistic, burden on auditors."[14]

Conclusion

The SEC certainly felt that it was unethical and illegal for KPMG to convince Miller's management to change the accounting treatment to a business combination from an asset acquisition. Ironically, a small, now defunct CPA firm initially made the right call that the transaction was an asset acquisition, but then allowed Miller to overvalue the assets and record a bargain purchase gain, but a Big-4 audit firm tried to reverse the correct accounting decision. This article provides numerous evidence that the transaction was an asset acquisition, and a bargain purchase gain was not available to Miller. Miller and KPMG clearly engaged in abusive earnings management. Without the much higher reserve valuation and the

---

[8] For more details see Christine Cheng and D.L. Crumbley, Measuring Damages in Federal Securities Fraud Cases: A Herculean Task, *J. of Forensic and Investigative Accounting*, Jan–June 2016, pp. 1–17.
[9] Sarath, Bharat. 2019. When do managers tell the truth about Bargain Purchase Gains? working paper, LSU Regional Workshop Series, March 1.
[10] Steven Lilien, Bharat Sarath, and Yan Yan, Fair value accounting, earnings management, and the case of bargain purchase gains, *Asian Review of Accounting*, April 24, 2020.
[11] Justin Mikulka, How Third-Party Auditors Make Oil Industry Fraud Possible, *DeSmog*, June 3, 2021.
[12] B. Olson, R. Elliott, and C.M. Matthews, Fracking's Secret Problem – Oil Wells Aren't Producing as Much as Forecast, *Wall Street Journal*, January 2, 2019.
[13] G.T. Olsen, W.J. Lee, and T.A. Blasingame, Reserve Overbooking: The Problem We Are Finally Going to Talk About, *SPE Economics & Management*, April 2011.
[14] B. E. Christensen, S.M. Grover, and D.A. Wood, Extreme Estimation Uncertainty in Fair Value Measures: Implications for Audit Assurance, *Current Issues in Auditing*, 2012, 31(1): 127-146.

huge bargain purchase gain, Miller may have remained a penny stock. Forensic accountants have a role to play in litigation cases involving fraud disputes in accounting reports.

Appendix A

The SEC asked Miller to respond to numerous questions, including requests about calculations of the reserves and the bargain purchase gain. The following are some written excerpts from a correspondence dated May 9, 2011, from Paul Boyd, a CPA and CFO of Miller, to respond to requests for explanations on numerous points by the Division of Corporation Finance of the Securities and Exchange Commission.

5. We note your acquisition on December 10, 2009, of the Alaskan assets of Pacific Energy Resources, ("Pacific Energy") which were valued at more than $479 million through a Delaware Chapter 11 bankruptcy proceeding. We note the acquisition included $215 million in proven energy reserves, $122 million in probable energy reserves and $31 million in possible energy reserves, providing total reserves of $368 million. Please provide the following information:

   - Who performed the valuation of these reserves;
   - A detailed analysis of how the value of each component of acquired reserves was determined;
   - Tell us and disclose the values of the remaining assets acquired that make up the balance of the total amount of $479 million;
   - The total consideration you paid for the asset acquisition;
   - The calculation and you're accounting for the bargain purchase gain in the amount of $274,821,626.

Response:

- Ralph E. Davis Associates, Inc., an independent petroleum engineering firm, performed the evaluation of the oil and natural gas reserves. Beecher Carlson, a third-party valuation specialist, performed the appraisal of the fixed assets.
- Proved Producing Reserves estimates were made generally using performance methods, the resultant values were then compared to volumetric calculations for reasonableness. Proved Behind Pipe and Proved Undeveloped Reserves were determined volumetrically. Proved Behind Pipe Reserves are from reservoirs that have either been tested or have produced previously. Proved Undeveloped Reserves are either twin wells to previously drilled, tested wells or are one location offsets to producing wells. Probable Reserves are volumetrically determined and are generally one additional location from producing wells. Possible reserves are from locations one location out from probable locations.
- Assets acquired consisted of the following:

Oil and Gas Properties	$	368,035,281
Restricted Cash		1,789,995
Inventory		212,228
Fixed Assets		110,516,500
Total	$	480,554,004

- Total consideration paid for the assets consisted of the following:

Cash paid	$	2,250,000
FV of Equity Issued		2,071,657
Cure amounts (payables)		1,001,252
Total	$	5,322,909

- Calculation of the bargain purchase gain is as follows:

Inventory	$	212,228
Fixed Assets		110,516,500
Oil & Gas Properties		368,035,281
Restricted Cash		1,789,995
Asset Retirement Liability		(15,289,994)
Accounts Payable		(2,230,057)
Cash paid at closing		(2,250,000)
FV of Equity Issued		(2,071,657)
Pre-tax Gain	$	458,712,296
Deferred taxes		(184,703,207)
Net Gain	$	274,009,089

The gain of $274,821,626 disclosed in the footnote was not the actual gain recorded, which was $274,009,089. The $812,537 difference relates to closing costs recorded, but not accurately disclosed in the footnote. We will modify the footnote presentation in future filings.

6. We note as a result of accounting records not being maintained on an adequate basis to carve out historical operational results on the specified acquired assets, the resulting assets and liabilities were deemed not to have been a separate business for purposes of preparing pro forma financials with historical results for the past year or a related stub period. Please provide more analysis on your conclusion this acquisition was not a separate business and should be accounted as an asset acquisition. Tell us specifically how long the oil and gas producing assets were not operational prior to acquisition and the period of time accounting records were not maintained. We note in addition to the oil and gas properties, a significant amount of onshore and offshore production facilities was also acquired. Tell us in more detail what is included in the fixed assets acquired in the amount of $110,516,500.

Response:

As we disclosed on page 39 (Recent Accounting Pronouncements) of the April 30, 2010, Form 10-K, we accounted for each of our fiscal 2010 acquisitions, including CIE, as business combinations, and applied the provisions of ASC Topic 805-20. We acknowledge that our description of the transaction in footnote six is confusing due to the fact that we described the transaction as an "acquisition of certain assets," and will clarify this in future filings.

In November 2009, the Company acquired the Alaska assets from a bankruptcy proceeding whereby certain assets of Pacific Energy were permitted by the bankruptcy court to be sold in pieces. The Pacific Energy estate had been abandoned as of September 10, 2009. The Pacific Energy administrative staff, including the accounting personnel and its offices had largely been dismantled by the time the Company had begun its due diligence in late October 2009. In December 2009, we had a telephone conversation with the former Chief Financial Officer of Pacific Energy, who informed us that his accounting systems were no longer operational, could not be accessed and that he would not be able to provide any historical accounting records for the acquired assets. He did not elaborate on the length of time Pacific Energy's accounting systems were not operational, and it was clear that he was not going to aid in obtaining historical financial information. We do not know for certain how long accounting records were not maintained, however, based on our due diligence procedures we estimate that there was at least a four-month period where no financial records were maintained.

The operations on the Alaska oil and gas wells had ceased production by August 31, 2009, and had not been fully operational for months according to the limited information provided to us during our due diligence. We subsequently determined that several of the wells, which were operational for a period of time with Pacific Energy, had become inoperable as the well casings had collapsed and would require rework. In addition, our Osprey offshore drilling platform ("Osprey Platform") ceased production in July 2009 and was inoperative, as its oil wells all had failed pumps and/or casing problems which required a workover or drilling rig to repair, and the drilling rig had been removed from the Osprey Platform. As a result, none of the oil wells supported by the offshore drilling platform could resume production without the substantial investment required to refurbish the Osprey Platform and its pipelines with a drilling rig.

10. We note you estimate that the agreement with Alaska DNR obligates you to $35 million in capital funding commitments, you will need up to approximately $67.4 million (page 29) associated with obligations arising from your purchase of the Alaskan assets, and your third-party reserve report presents $50 million in proved property development costs.

Response:

The $67.4 million figure included the $35 million in estimated development funding, plus the estimated $32.4 million for asset retirement obligations.