US ENERGY CORP
Form 10-Q
November 10, 2008

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 quarter ended September 30, 2008 or

o Transition report pursuant to section 13 or 15(d) of the Securities Exchange Act of 1934
For the transition period from ___________ to ____________

Commission file number 0-6814

U.S. ENERGY CORP.
(Exact Name of Company as Specified in its Charter)

Wyoming (State or other jurisdiction of incorporation or organization)	83-0205516 (I.R.S. Employer Identification No.)
877 North 8th West, Riverton, WY (Address of principal executive offices)	82501 (Zip Code)
Company's telephone number, including area code:	(307) 856-9271

Not Applicable
Former name, address and fiscal year, if changed since last report

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

YES o NO x

Indicate by check mark if the registrant is not required to file reports to Section 13 or Section 15(d) of the Act.

YES o NO x

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 Company was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

YES x NO o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange act.

Large accelerated filer o Accelerated filer x Non-accelerated filer o

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

YES o NO x

APPLICABLE ONLY TO ISSUERS INVOLVED IN BANKRUPTCY
PROCEEDINGS DURING THE PRECEDING FIVE YEARS:

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Section 12, 13, or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court.

YES o NO o

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Outstanding Shares at November 6, 2008
Common stock, $.01 par value	22,389,050

U.S. ENERGY CORP. and SUBSIDIARIES

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PART I. FINANCIAL INFORMATION

ITEM 1. Financial Statements

U.S. ENERGY CORP.
CONDENSED BALANCE SHEETS
ASSETS
(Unaudited)

	September 30, 2008	December 31, 2007
CURRENT ASSETS:		
Cash and cash equivalents	$ 1,146,900	$ 72,292,200
Marketable securities		
Held to maturity - treasuries	68,561,100	--
Available for sale securities	892,800	480,200
Accounts receivable		
Trade	120,400	171,700
Reimbursable project costs	128,500	782,100
Dissolution of subsidiaries	--	197,600
Income taxes	5,316,500	902,900
Restricted investments	4,928,400	6,624,700
Assets held for sale	--	1,112,600
Real estate held for sale	590,700	--
Deferred tax assets	601,800	59,700
Prepaid expenses and other current assets	101,600	105,200
Total current assets	82,388,700	82,728,900
PROPERTIES AND EQUIPMENT:	66,475,500	52,785,200
Less accumulated depreciation,		
depletion and amortization	(4,873,800)	(4,691,700)
Net properties and equipment	61,601,700	48,093,500
OTHER ASSETS:		
Restricted investments	367,800	375,500
Deposits and other	548,700	206,500
Total other assets	916,500	582,000
Total assets	$ 144,906,900	$ 131,404,400

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

U.S. ENERGY CORP.
CONDENSED BALANCE SHEETS
LIABILITIES AND SHAREHOLDERS' EQUITY
(Unaudited)

	September 30, 2008	December 31, 2007
CURRENT LIABILITIES:		
Accounts payable	$ 1,334,800	$ 1,589,600
Accrued compensation	863,900	275,200
Short term construction debt	16,433,800	5,489,000
Current portion of long-term debt	71,900	71,900
Other current liabilities	724,800	667,500
Total current liabilities	19,429,200	8,093,200
LONG-TERM DEBT, net of current portion	133,800	190,500
DEFERRED TAX LIABILITY	8,950,700	6,928,800
ASSET RETIREMENT OBLIGATIONS	141,300	133,400
OTHER ACCRUED LIABILITIES	855,300	958,600
PREFERRED STOCK,		
$.01 par value; 100,000 shares authorized		
No shares issued or outstanding	--	--
SHAREHOLDERS' EQUITY:		
Common stock, $.01 par value; unlimited shares		
authorized; 23,018,825 and 23,592,493		
shares issued, respectively	230,200	235,900
Additional paid-in capital	96,239,900	96,560,100
Accumulated surplus	19,385,300	19,050,900
Unrealized loss on marketable securities	(458,800)	(256,500)
Unallocated ESOP contribution	--	(490,500)
Total shareholders' equity	115,396,600	115,099,900
Total liabilities and shareholders' equity	$ 144,906,900	$ 131,404,400

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

U.S. ENERGY CORP.
CONDENSED STATEMENTS OF OPERATIONS
(Unaudited)

	Three months ended September 30, 2008	Three months ended September 30, 2007	Nine months ended September 30, 2008	Nine months ended September 30, 2007
OPERATING REVENUES:				
Remington Village real estate	$ 497,100	$ --	$ 873,100	$ --
Other real estate	66,500	569,400	121,800	738,600
Management fees and other	5,100	56,800	51,700	198,000
	568,700	626,200	1,046,600	936,600
OPERATING COSTS AND EXPENSES:				
Remington Village real estate	232,100	--	474,400	--
Other real estate	78,600	80,300	237,200	247,700
Mineral holding costs	1,208,600	238,300	2,282,100	1,353,700
General and administrative	1,697,500	2,150,200	5,968,600	11,469,500
	3,216,800	2,468,800	8,962,300	13,070,900
LOSS BEFORE INVESTMENT AND PROPERTY TRANSACTIONS	(2,648,100)	(1,842,600)	(7,915,700)	(12,134,300)
OTHER INCOME & (EXPENSES):				
(Loss) gain on sales of assets	12,400	400	(16,600)	1,822,600
Loss on sale of marketable securities	--	(2,227,000)	--	(8,318,400)
Gain (loss) on foreign exchange	--	(72,600)	--	430,000
Gain on sale of uranium assets	--	--	--	111,728,200
Loss from dissolution of subsidiaries	--	(78,700)	--	(78,700)
Dividends	--	17,100	--	22,700
Interest income	324,100	1,195,600	1,174,500	2,047,000
Interest expense	(146,300)	(14,000)	(254,100)	(63,400)
	190,200	(1,179,200)	903,800	107,590,000
(LOSS) GAIN BEFORE MINORITY INTEREST, PROVISION FOR INCOME TAXES AND DISCONTINUED OPERATIONS	(2,457,900)	(3,021,800)	(7,011,900)	95,455,700
MINORITY INTEREST IN LOSS (GAIN) OF CONSOLIDATED SUBSIDIARIES	--	147,200	--	(3,551,400)
(LOSS) GAIN BEFORE PROVISION FOR INCOME TAXES AND DISCONTINUED OPERATIONS	(2,457,900)	(2,874,600)	(7,011,900)	91,904,300

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

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U.S. ENERGY CORP.
CONDENSED STATEMENTS OF OPERATIONS
(Unaudited)

	Three months ended September 30, 2008	Three months ended September 30, 2007	Nine months ended September 30, 2008	Nine months ended September 30, 2007
INCOME TAXES:				
Current benefit from (provision for)	1,881,000	1,995,200	4,003,200	(18,625,100)
Deferred benefit from (provision for)	(819,000)	526,400	(1,563,400)	(14,512,700)
	1,062,000	2,521,600	2,439,800	(33,137,800)
(LOSS) GAIN FROM CONTINUING OPERATIONS	(1,395,900)	(353,000)	(4,572,100)	58,766,500
DISCONTINUED OPERATIONS				
Loss from discontinued operations	(210,800)	(397,000)	(501,100)	(1,539,300)
Gain on sale of discontinued operations (net of taxes)	5,407,600	--	5,407,600	--
	5,196,800	(397,000)	4,906,500	(1,539,300)
NET (LOSS) INCOME	$ 3,800,900	$ (750,000)	$ 334,400	$ 57,227,200
PER SHARE DATA				
Basic (loss) earnings from continuing operations	$ (0.06)	$ (0.02)	$ (0.19)	$ 2.94
Basic earnings (loss) from discontinued operations	0.22	(0.02)	0.20	(0.08)
Basic (loss) earnings per share	$ 0.16	$ (0.04)	$ 0.01	$ 2.86
Diluted (loss) earnings from continuing operations	$ (0.06)	$ (0.02)	$ (0.19)	$ 2.68
Diluted (loss) earnings from discontinued operations	0.22	(0.02)	0.20	(0.07)
Diluted (loss) earnings per share	$ 0.16	$ (0.04)	$ 0.01	$ 2.61
BASIC WEIGHTED AVERAGE SHARES OUTSTANDING	23,505,340	20,558,882	23,629,490	20,024,465
DILUTED WEIGHTED AVERAGE SHARES OUTSTANDING	23,505,340	20,558,882	23,629,490	21,901,936

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

U.S. ENERGY CORP.
STATEMENTS OF CASH FLOWS
(Unaudited)

	For the nine months ended September 30, 2008	2007
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 334,400	$ 57,227,200
Gain on the sale of SGMI stock	(5,407,600)	--
Loss from discontinued operations	501,100	1,539,300
Net (loss) gain from continuing operations	(4,572,100)	58,766,500
Reconcile net loss from continuing operations		
to net cash used in operations		
Minority interest in the loss of subsidiaries	--	3,551,400
Depreciation	688,500	302,700
Accretion of asset retirement obligations	--	6,900
Accretion of discount on treasury investments	(991,900)	--
Noncash interest income	--	(1,274,000)
Income tax receivable	(3,399,100)	--
Deferred income taxes	1,563,400	14,512,700
Income tax payable	--	1,569,700
Gain on sale of assets to Uranium One	--	(111,728,100)
Loss (gain) on sale of assets	16,600	(1,860,800)
Gain on foreign exchange	--	(443,300)
Loss on sales of marketable securities	--	8,318,400
Warrant extension and repricing	--	156,500
Noncash compensation	2,135,400	1,089,700
Noncash services	23,600	--
Net changes in assets and liabilities:	186,700	345,700
NET CASH USED IN OPERATING ACTIVITIES	(4,348,900)	(26,686,000)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from sale of marketable securities	$ --	$ 92,250,700
Proceeds from sale of uranium assets	--	14,022,700
Proceeds from sale of property and equipment	1,097,000	1,294,200
Acquisition & development of real estate	(11,001,400)	(6,595,200)
Acquisition of unproved oil & gas properties	(4,533,600)	(2,894,100)
Acquisition & development		
of unproved mining claims	(517,800)	(224,200)
Acquisition of property and equipment	(55,700)	(5,584,300)
Maturities of treasury investments	206,320,000	--
Acquisitions of treasury investments	(273,889,200)	(70,000,000)
Net change in restricted investments	1,704,000	--
Net change in notes receivable	--	560,500
Net change in investments in affiliates	--	(79,500)
NET CASH (USED IN) PROVIDED		
BY INVESTING ACTIVITIES	(80,876,700)	22,750,800

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

U.S. ENERGY CORP.
STATEMENTS OF CASH FLOWS
(Unaudited)

	For the nine months ended September 30, 2008	2007
CASH FLOWS FROM FINANCING ACTIVITIES:		
Issuance of common stock	1,527,600	2,284,100
Issuance of subsidiary stock	--	342,000
Payment of cash dividend	--	(2,108,300)
Restricted investment for credit facility	--	(4,725,000)
Tax benefit from the exercise of stock options	170,400	1,415,400
Proceeds from long term debt	10,944,800	164,100
Repayments of long term debt	(56,700)	(1,089,200)
Stock buyback program	(2,831,500)	(1,047,300)
NET CASH PROVIDED BY FINANCING ACTIVITIES	9,754,600	(4,764,200)
Net cash used in operating activities of discontinued operations	(76,500)	(1,415,100)
Net cash provided by (used in) investing activities of discontinued operations	4,402,200	(37,400)
NET DECREASE IN CASH AND CASH EQUIVALENTS	(71,145,300)	(10,151,900)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	72,292,200	16,973,500
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 1,146,900	$ 6,821,600
SUPPLEMENTAL DISCLOSURES:		
Income tax (received) paid	$ (944,900)	$ 15,640,000
Interest paid	$ 47,800	$ 63,800
NON-CASH INVESTING AND FINANCING ACTIVITIES:		
Issuance of subsidiary stock to acquire mining claims	$ --	$ 33,700
Receipt of marketable securities from the sale of assets	$ --	$ 99,400,600
Unrealized loss/gain	$ 458,800	$ 195,800

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

U.S. ENERGY CORP. & SUBSIDIARIES
Notes to Condensed Consolidated Financial Statements (Unaudited)

1) Basis of Presentation

The Condensed Balance Sheet as of September 30, 2008, the Condensed Statements of Operations for the three and nine months ended September 30, 2008 and 2007 and the Condensed Statements of Cash Flows for the nine months ended September 30, 2008 and 2007, have been prepared by the Company without audit. The Condensed Consolidated Balance Sheet at December 31, 2007 was derived from financial statements audited by Moss Adams, LLP, independent public accountants, as indicated on their report for the year ended December 31, 2007 (which report is not included in this Form 10-Q Report). In the opinion of the Company, the accompanying condensed financial statements contain all adjustments (consisting of only normal recurring adjustments) necessary to present fairly the financial position of the Company as of September 30, 2008 and December 31, 2007, the results of operations for the three and nine months ended September 30, 2008 and 2007 and cash flows for the nine months ended September 30, 2008 and 2007.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted. It is suggested that these financial statements be read in conjunction with the Company's December 31, 2007 Form 10-K. The results of operations for the periods ended September 30, 2008 and 2007 are not necessarily indicative of the operating results for the full year.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates based on certain assumptions. These estimates and assumptions 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 revenues and expenses during the reporting period.

2) Principles of Consolidation

The consolidated Balance Sheet of the Company at December 31, 2007 included the accounts of the Company and Sutter Gold Mining Inc. (“SGMI”) which was owned 54.4% by the Company at December 31, 2007. All material inter-company profits, transactions and balances were eliminated. During the nine months ended September 30, 2008, the Company sold the majority of its shares of SGMI and SGMI operations have been reclassified as discontinued operations (see Note 16).

The consolidated statement of operation and statement of cash flows of the Company as of September 30, 2007 also include the accounts of its then majority-owned or controlled subsidiaries Plateau Resources Limited, Inc. (“Plateau”) (100%); Crested Corp. (“Crested”) (70.1%); SGMI (54.4%), and the USECC Joint Venture ("USECC"), a consolidated joint venture which was equally owned by the Company and Crested. Subsequent to September 30, 2007 all these subsidiaries and affiliated companies were liquidated or merged into the Company.

U.S. ENERGY CORP. & SUBSIDIARIES
Notes to Condensed Consolidated Financial Statements (Unaudited)
(Continued)

3) Recent Accounting Pronouncements

SFAS 141R In December 2007, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 141(R), "Business Combinations" ("SFAS 141(R)"), to replace SFAS 141, "Business Combinations". SFAS 141(R) requires use of the acquisition method of accounting, defines the acquirer, establishes the acquisition date and broadens the scope to all transactions and other events in which one entity obtains control over one or more other businesses. This statement is effective for financial statements issued for fiscal years beginning on or after December 15, 2008 with earlier adoption prohibited. While the Company does not expect that the adoption of SFAS 141(R) to have a material impact to its consolidated financial statements for transactions completed prior to December 31, 2008, the impact of the accounting change could be material for business combinations which may be consummated subsequent thereto.

SFAS 157 In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements" ("SFAS 157"), which defines fair value, establishes a framework for measuring fair value under generally accepted accounting principles and expands disclosures about fair value measurements. SFAS 157 applies to other existing accounting pronouncements that require or permit fair value measurements, the FASB having previously concluded in those accounting pronouncements that fair value is the relevant measurement attribute. While SFAS 157 does not require any new fair value measurements, its application may change the current practice for fair value measurements. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. On February 8, 2008, the FASB issued FSP FAS 157-2, "Effective Date of FASB Statement No. 157", which delays the effective date of SFAS 157 for nonfinancial assets and liabilities to fiscal years beginning after November 15, 2008. The adoption of SFAS 157 for financial assets and liabilities in the first quarter of 2008 had no impact on our consolidated financial statements. The Company is currently evaluating the impact of SFAS 157 for non-financial assets and liabilities.

SFAS 159 In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities" ("SFAS 159") which permits entities to choose to measure many financial instruments and certain other items at fair value that are not currently required to be measured at fair value. SFAS 159 will be effective for the Company's current fiscal year ending December 31, 2008. The effect of adopting this statement did not have a material impact on the Company's consolidated financial position, results of operations or cash flows.

SFAS 160 In December 2007, the FASB issued SFAS No. 160, "Non controlling Interests in Consolidated Financial Statements"—an amendment of Accounting Research Bulletin No. 51, ("SFAS 160"). SFAS 160 establishes accounting and reporting standards for the non controlling interest in a subsidiary and for the retained interest and gain or loss when a subsidiary is deconsolidated. This statement is effective for financial statements issued for fiscal years beginning on or after December 15, 2008 with earlier adoption prohibited. The Company is currently evaluating the impact of SFAS 160 on its financial statements.

The Company has reviewed other recently issued accounting pronouncements and does not believe that any of those pronouncements will have a material effect on the Company's financial position or results of operations when adopted.

U.S. ENERGY CORP. & SUBSIDIARIES
Notes to Condensed Consolidated Financial Statements (Unaudited)
(Continued)

4) Stock Based Compensation

Stock Options - The Company accounts for all stock-based compensation pursuant to SFAS No. 123(R), “Share Based Payment” which requires the recognition of the fair value of stock-based compensation in operations. Stock-based compensation to all employees primarily consists of stock options. Stock options are granted to employees at exercise prices equal to the fair market value of the Company’s stock at the dates of grant.

Options expire 90 days after the employee voluntarily terminates their employment with the Company or twelve months after retirement, disability or death and vest over various time periods established at time of grant. The Company recognizes the stock-based compensation expense over the requisite service period of the individual grantees, which generally equals the vesting period. The Company provides newly issued shares to satisfy stock option exercises (see Note 13).

The Company also issues shares of Common Stock to four officers of the Company under the 2001 Stock Compensation Plan as amended by vote of the shareholders on June 22, 2007. Under the terms of the 2001 Stock Compensation Plan each of the four officers is issued 5,000 shares on a quarterly basis and the Company reimburses the officers any taxes due as a result of the issuance of the shares. The officers have agreed not to sell, pledge or in any other way encumber the shares issued under the 2001 Stock Compensation Plan prior to their retirement, disability or death. These shares are a portion of the overall compensation package of the executives and are in lieu of additional cash compensation being paid to the officers (see Note 13).

5) Properties and Equipment

The components of Properties and Equipment at September 30, 2008 are oil and gas properties, mining properties, rental properties and buildings land and equipment.

	Cost	Accumulated Amortization Depletion and Depreciation	Net Book Value
Oil & Gas properties	$ 7,468,400	$ -	$ 7,468,400
Mining properties	21,566,100	-	21,566,100
Rental properties	22,681,800	(256,400)	22,425,400
Buildings, land and equipment	14,759,200	(4,617,400)	10,141,800
Totals	$ 66,475,500	$ (4,873,800)	$ 61,601,700

U.S. ENERGY CORP. & SUBSIDIARIES
Notes to Condensed Consolidated Financial Statements (Unaudited)
(Continued)

The Company evaluates assets for impairment when events or circumstances indicate that recorded values may not be recoverable. There were no impairments for the three and nine months ended September 30, 2008 and 2007. Mining properties of $21,566,100 are the result of the allocation of the purchase price associated with the merger of Crested Corp. into the Company during the fourth quarter of 2007 as well as expenditures the Company incurred in the permitting process related to the Lucky Jack molybdenum property ("Lucky Jack") in Colorado. The Company is in the process of conducting a valuation of the allocation of the purchase price under SFAS 141 which it anticipates having completed during the fourth quarter of 2008. The Company incurred $1,238,600 in permitting and engineering studies relating to the Lucky Jack property, which were capitalized, during the nine months ended September 30, 2008. During the nine months ended September 30, 2008 the Company abandoned certain options on uranium leases it held with a book value of $31,100 as the Company saw no economic value in retaining the leases. Land, buildings, improvements, machinery and equipment are carried at cost. Depreciation of buildings, improvements, machinery and equipment is provided principally by the straight-line method over estimated useful lives ranging from 3 to 45 years. Following is a breakdown of the lives over which assets are depreciated.

Machinery and equipment		
	Office Equipment	3 to 5 years
	Aircraft	10 years
	Field Tools and Hand Equipment	5 to 7 years
	Vehicles and Trucks	3 to 7 years
	Heavy Equipment	7 to 10 years
Buildings and improvements		
	Service Buildings	20 years
	Multifamily Housing	25 years
	Corporate Headquarters' Building	45 years

6) Marketable Securities

The Company accounts for its marketable securities as (1) held-to-maturity, (2) available-for-sale and (3) trading. The Company holds short-term securities which have maturities of greater than three months but less than one year from the date of purchase; these securities are classified as held-to-maturity based on the Company's intent to hold such securities to the maturity date. All held-to-maturity securities are U.S. Government securities and are stated at amortized cost, which approximates fair market value. Income related to these securities is reported as a component of interest income. The Company's available-for-sale securities are carried at fair value with net unrealized gain or (loss) recorded as a separate component of shareholders' equity. If a decline in fair value of held-to-maturity securities is determined to be other than temporary, the investment is written down to fair value. Based on the Company's intent to sell the securities, its equity securities are reported as trading securities.

U.S. ENERGY CORP. & SUBSIDIARIES
Notes to Condensed Consolidated Financial Statements (Unaudited)
(Continued)

7) Other Comprehensive Income (Loss)

Unrealized gains and losses on investments, available-for-sale securities, are excluded from net income but are reported as comprehensive income on the Condensed Consolidated Balance Sheets under Shareholders' equity. The following table reconciles net loss/gain to comprehensive loss/gain:

	For the three months September 30,		For the nine months ending September 30,	
	2008	2007	2008	2007
Net gain/(loss)	$ 3,800,900	$ (750,000)	$ 334,400	$ 57,227,200
Comprehensive loss from the unrealized loss on marketable securities	(110,400)	(4,335,800)	(284,900)	(324,000)
Reclassification adjustment for gains included in net income	--	--	--	(305,100)
Deferred income taxes on marketable securities	39,000	1,410,400	83,600	127,300
Comprehensive gain/(loss)	$ 3,729,500	$ (3,675,400)	$ 133,100	$ 56,725,400

8) Income Taxes

The income tax provision differs from the amounts computed by applying the statutory federal income tax rate to income from continuing operations before taxes. The reasons for these differences are as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
Book Income/(Loss) before Income Tax	$ 2,738,900	$ (3,271,600)	$ (2,105,400)	$ 90,365,000
Reverse income from discontinued operations	(5,196,800)		(4,906,500)	
Equity income from non consolidated tax sub		(160,100)		3,551,400
Add back losses from non consolidated tax subs		391,300		1,545,400
	(549,300)		(549,300)	

Tax impact of change in asset classification				
Prior year true-up and rate change	(171,400)	(265,100)	(171,400)	(265,100)
Permanent differences	411,200	(1,755,600)	1,028,700	(1,517,300)
Taxable (loss)/income before temporary differences	$ (2,767,400)	$ (5,061,100)	$ (6,703,900)	$ 93,679,400
Expected federal income tax expense (benefit) 35%	$ (968,500)	$ (1,771,500)	$ (2,346,300)	$ 32,787,800
Federal deferred income tax expense (benefit)	$ 819,000	$ (526,400)	$ 1,563,400	$ 14,512,700
Federal current expense (benefit)	(1,787,500)	(1,245,200)	(3,909,700)	18,275,100
Total federal income tax expense (benefit)	(968,500)	(1,771,600)	(2,346,300)	32,787,800
Current state income tax expense net of federal tax benefit	(93,500)	(750,000)	(93,500)	350,000
Total provision (benefit) from Continuing Operations	$ (1,062,000)	$ (2,521,600)	$ (2,439,800)	$ 33,137,800

U.S. ENERGY CORP. & SUBSIDIARIES
Notes to Condensed Consolidated Financial Statements (Unaudited)
(Continued)

Current taxes receivable at September 30, 2008 is comprised of $5,223,000 of federal income taxes and $93,500 of state income taxes. The amount of current federal taxes receivable has been increased by $170,400 benefit from the exercise of pre-FAS 123R nonqualified stock options and warrants which result in an increase to paid in capital and $1,193,600 benefit related to the sale of discontinued operations. At December 31, 2007, current taxes receivable was $902,900.

The tax impact of change in asset classification relates to the Company's investment in shares of Sutter Gold Mining, Inc. that it owns at September 30, 2008. When this asset was previously accounted for as a consolidated subsidiary, no deferred tax asset for the excess of tax basis over book basis was recognized. As this investment is now being treated as a marketable security, a deferred tax asset is recognized in the current period.

The components of deferred taxes as of September 30, 2008 and December 31, 2007 are as follows:

	September 30, 2008	December 31, 2007
Current deferred tax assets:		
Tax basis in excess of book	$ 439,300	$ -
Non-deductible reserves and other	162,500	59,700
Total net current deferred tax assets/(liabilities)	$ 601,800	$ 59,700
Non-current deferred tax assets:		
Deferred compensation	$ 626,800	$ 436,300
Accrued reclamation	49,500	38,500
Tax basis in excess of book	-	200,400
Total noncurrent deferred tax assets	676,300	675,200
Non-current deferred tax liabilities:		
Book basis in excess of tax basis	(9,616,100)	(7,604,000)
Accrued reclamation	(10,900)	
Total deferred tax liabilities	(9,627,000)	(7,604,000)
Total net non-current deferred tax assets/(liabilities)	$ (8,950,700)	$ (6,928,800)

A valuation allowance for deferred tax assets is required when it is more likely than not that some portion or all of the deferred tax assets will not be realized. No valuation allowance is provided at September 30, 2008 and December 31, 2007 as the Company believes that it is more likely than not that the deferred tax assets will be utilized in future years.

During the nine months ended September 30, 2008, net current deferred tax assets increased by $542,100 and net non-current deferred tax liabilities increased by $2,021,900. The total change in net deferred tax liabilities was an increase of $1,479,800, comprised of a deferred income tax expense of $1,563,400 and the recognition of other comprehensive income in the amount of $83,600 resulting from the tax expense related to the mark to market of available for sale securities. The book basis in excess of tax basis in the schedule above relates primarily to the $7,287,300 difference created from the excess of the purchase price over the carrying value of the assets acquired in the purchase of the remaining minority interest of Crested Corp in 2007.

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The Company's practice is to recognize interest and/or penalties related to income tax matters in income tax expense. The Company had no accrued interest or penalties at September 30, 2008 or December 31, 2007.

On January 1, 2007 the Company adopted FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes" ("FIN 48"). Pursuant to FIN 48, the Company identified and evaluated any potential uncertain tax positions. The Company has concluded that there are no uncertain tax positions requiring recognition in the financial statements.

The Internal Revenue Service has audited the Company's tax returns through the year ended May 31, 2000. The Company's income tax liabilities are settled through fiscal 2000.

9) Assets Held for Sale

Long lived assets and liabilities that will be sold within one year of the financial statements are classified as current. At September 30, 2008 and December 31, 2007, the Company reported $590,700 and $1,112,600, respectively, in assets held for sale. The Asset Held for Sale at September 30, 2008 consisted of undeveloped real estate in Riverton, Wyoming and at December 31, 2007 an aircraft which was sold during the nine months ended September 30, 2008.

10) Earnings Per Share

The Company presents basic and diluted earnings per share in accordance with the provisions of SFAS No. 128, "Earnings per Share". Basic earnings per common share are based on the weighted average number of common shares outstanding during the period. Diluted earnings per share is computed based on the weighted average number of common shares outstanding adjusted for the incremental shares attributed to outstanding options and warrants to purchase common stock, if dilutive. As the results of continuing operations for the three and nine months ended September 30, 2008 were losses, dilutive options and warrants were excluded from the diluted calculation because they would be anti-dilutive. Dilutive options and warrants excluded at September 30, 2008 totaled 5,204,461. (See Note 13) Dilutive options and warrants totaled 5,867,729 at September 30, 2007.

11) Debt

At September 30, 2008, debt consists of debt related to the construction of the Remington Village multifamily property and the purchase of equipment at various interest rates and due dates:

Short-term construction debt	$ 16,433,800
Current portion of long-term debt	71,900
Long-term debt	133,800
Total	$ 16,639,500

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(Continued)

12) Asset Retirement Obligations

The Company accounts for the reclamation of its mineral properties pursuant to SFAS No. 143, “Accounting for Asset Retirement Obligation.” Under the provisions of this statement, the Company records the estimated fair value of the reclamation liability on its mineral properties as of the date that the liability is incurred with a corresponding increase in the property’s book value. Actual costs could differ from those estimates. The Company deducts any actual funds expended for reclamation from the asset retirement obligations during the quarter in which it occurs. The reclamation liabilities are reviewed each quarter to determine whether estimates for the total asset retirement obligation are sufficient to complete the reclamation work required. Asset retirement obligations at September 30, 2008 are for reclamation obligations related to the Lucky Jack project and a Gulf Coast gas well.

The following is a reconciliation of the total liability for asset retirement obligations (unaudited):

	For the nine months ending September 30,	
	2008	2007
Balance January 1,	$ 133,400	$ 124,400
Accretion of estimated ARO	6,600	6,900
Initial valuation of ARO	24,600	--
Deconsolidation of Sutter Gold	(23,300)	--
Balance September 30,	$ 141,300	$ 131,300

13) Shareholders’ Equity

Stock Option Plans

The Board of Directors adopted, and the shareholders approved, the U.S. Energy Corp. 2001 Incentive Stock Option Plan (the "2001 ISOP") for the benefit of the Company's employees. The 2001 ISOP reserves for issuance shares of the Company’s common stock equal to 25% of the Company’s shares of common stock issued and outstanding as of June 22, 2007. The 2001 ISOP has a term of 10 years from date of initial adoption.

On September 22, 2008, the Board of Directors issued 562,500 new options under the 2001 ISOP to officers and employees of the Company. All options issued on September 22, 2008 were granted at the closing price of $2.52 on the date of grant and vest over three years in equal annual installments beginning September 22, 2009.

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The weighted average remaining contractual term and aggregate intrinsic value of all employee options at September 30, 2008 was 6.22 years and $273,300, respectively. At September 30, 2008, 1,585,829 of the options granted were not vested. During the three and nine months ending September 30, 2008, the Company recognized $354,300 and $1,042,300, respectively in compensation expense related to employee options and will recognize an additional $4,294,000 over the remaining vesting period of seven years. During the three and nine months ended September 30, 2007, the Company recognized $326,000 and $334,900 in compensation expense related to employee stock options. The Company computes the fair values of its options granted using the Black-Scholes pricing model. The options issued in 2008 were valued under Black-Scholes using a risk free interest rate of 3.23%, expected life of 6 years and expected volatility of 56.5%. Cumulative compensation cost recognized in pro forma net income or loss with respect to options that are forfeited prior to vesting is adjusted as a reduction of pro forma compensation expense in the period of forfeiture.

Warrants to Others

From time to time the Company issues stock purchase warrants to non-employees for services.

During the nine months ended September 30, 2008, the Company issued 40,000 warrants to a consultant. The warrants were issued at the closing price of $2.81 on the date of grant, vest over a four year period and expire four years from the date of grant. The 130,000 warrants issued to the Independent Directors and one Advisory Board member during the three and nine months ended September 30, 2008 were issued at the closing price of $2.52 on the date of grant, vest over a three year period and expire 10 years from the date of grant. The Company recorded $15,900 and $23,600 in expense during the three and nine months ended September 30, 2008 for warrants issued to third parties and $116,300 in expense associated with warrants issued during the nine months ended September 30, 2007. The Company will recognize an additional $193,300 in expense over the life of the warrants issued during the nine months ended September 30, 2008.

The following table represents the activity in employee stock options and non-employee stock purchase warrants for the nine months ended September 30, 2008:

	September 30, 2008	
	Employee Stock Options	Stock Purchase Warrants