

**ALLIED ENERGY, INC. AND SUBSIDIARIES
FINANCIAL STATEMENTS (UNAUDITED)**

December 31, 2011

TABLE OF CONTENTS

Consolidated Balance Sheets	F-2
Consolidated Statements of Operations	F-3
Consolidated Statements of Changes in Stockholder's Equity	F-4
Consolidated Statements of Cash Flows	F-5
Notes to the Unaudited Consolidated Financial Statements	F-6 - 21

ALLIED ENERGY, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
as of December 31, 2011 and December 31, 2010
(UNAUDITED)

	December 31, 2011	December 31, 2010
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	3,942,216	\$ 3,406,298
Accounts receivable, net	990,044	241,507
Joint Interest Billing - In Progress	3,769,092	121,797
Employee loans	77,175	129,459
Inventory	22,431	45,817
Deferred income tax assets	537,267	108,089
Prepaid expenses and other current assets	6,870	76,009
Prefunding of Drilling Escrow Account	356,453	577,470
TOTAL CURRENT ASSETS	9,701,548	4,706,446
Investments	6,812	249,190
Property and equipment, net	5,421,268	6,535,029
Oil and gas properties, net	2,061,675	4,392,948
Drilling program syndications	230,034	205,546
Deferred Income Tax Asset	-	168,913
Deferred compensation	554,517	84,868
Employee Loans (Long Term Portion)	-	80,000
Deposits	-	11,930
Other assets	426,335	-
TOTAL ASSETS	\$ 18,402,188	\$ 16,434,870
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES		
Current maturities of notes payable	88,702	\$ 141,919.00
Accounts payable	1,264,615	3,214,556.00
Accrued liabilities	89,172	115,910
Current portion of accrued severance	259,448	265,872
Revenue payable	734,595	393,228
Deferred revenue	-	-
Income tax payable	1,444,221	207,077
TOTAL CURRENT LIABILITIES	3,880,752	4,338,563
Notes payable	1,755,480	1,738,146
Accrued severance, net of current portion	419,923	681,686
Deferred income tax liabilities	260,265	-
TOTAL LIABILITIES	6,316,420	6,758,395
Commitments and contingencies		
STOCKHOLDERS' EQUITY		
Series A preferred stock, \$0.01 par value, 10,000,000 shares authorized, 100,000 shares issued and outstanding as of June 30, 2011 and December 31, 2010, respectively	1,000	1,000
Common stock, \$0.001 par value, 200,000,000 shares authorized, 74,644,487 and 69,446,333 shares issued and outstanding as of June 30, 2011 and December 31, 2010	74,645	69,447
Additional paid-in capital	7,234,180	6,217,637
Treasury stock (858,900 shares)	(133,336)	(133,336)
Retained earnings	2,101,613	611,865
TOTAL STOCKHOLDERS' EQUITY ATTRIBUTABLE TO ALLIED ENERGY, INC. AND SUBSIDIARIES	9,278,102	6,766,613
Non-controlling interest	2,807,665	2,909,862
TOTAL STOCKHOLDERS' EQUITY	12,085,767	9,676,475
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	18,402,188	\$ 16,434,870

See accompanying notes to the unaudited consolidated financial statements

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

ALLIED ENERGY, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
For the years ended December 31,
(UNAUDITED)

	<u>2011</u>	<u>2010</u>
Revenues:		
Revenue		
Turnkey Drilling income	\$ 20,499,266	\$ 26,364,505
Turnkey Production income	\$ 547,587	\$ 1,153,576
Total Revenues	<u>21,046,852</u>	<u>27,518,081</u>
Cost of Drilling, Exploration, & Development	<u>16,707,560</u>	<u>18,973,151</u>
Gross Profit	<u>4,339,292</u>	<u>8,544,930</u>
Sales, General, & Administrative	<u>5,864,673</u>	<u>8,674,270</u>
Income/(Loss) from Operations	<u>(1,525,381)</u>	<u>(129,340)</u>
Other (Income) Expense:		
Gain on Sale of Real Estate Investment	32,729	
Gain on Sale of Oil & Gas producing property	6,001,071	
Dividend Income	101,991	
Interest Expense	(70,188)	(169,917)
Interest & Investment Income	2,712	30,815
Impairment of Drilling Program Syndications		-
Impairment of Oil and Gas Properties		-
Impairment of Investment		(126,993)
Other (Income) Expense:	<u>6,068,315</u>	<u>(266,095)</u>
Net Income/(Loss) Attributable to Minority Interest	<u>102,195</u>	<u>19,834</u>
Net Income/(Loss) before Provision for Income Taxes	<u>4,645,129</u>	<u>(375,601)</u>
Provision for Income Taxes	<u>1,479,000</u>	<u>(69,925)</u>
Net Income/(Loss) Attributable to Company	<u>\$ 3,166,129</u>	<u>\$ (305,676)</u>
Weighted Average Common Shares Outstanding	<u>72,181,831</u>	<u>68,124,285</u>
Earnings (Loss) per Share Outstanding	<u>\$ 0.0439</u>	<u>\$ (0.0045)</u>
Weighted Average Common Shares Outstanding - Fully Diluted	<u>92,179,177</u>	<u>91,313,631</u>
Earnings/(Loss) per Share - Fully Diluted	<u>\$ 0.0343</u>	<u>\$ (0.0033)</u>

See accompanying notes to the unaudited consolidated financial statements

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

ALLIED ENERGY, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY
For the year ended December 31, 2011
(UNAUDITED)

	Series A Convertible Preferred Stock, 10,000,000 Shares Authorized	Series A Convertible Preferred Stock, \$0.01 Par Value	Common Stock, 200,000,000 Shares Authorized	Common Stock, \$0.001 Par Value	Additional Paid-in Capital	Treasury Stock	Retained Earnings	Total Stockholders' Equity Attributable to Parent	Non- Controlling Interest	Total Stockholders' Equity
Balances, December 31, 2010	<u>100,001</u>	<u>\$ 1,000</u>	<u>69,446,333</u>	<u>\$ 69,447</u>	<u>\$ 6,217,637</u>	<u>\$ (133,336)</u>	<u>\$ 611,865</u>	<u>\$ 6,766,614</u>	<u>\$ 2,909,862</u>	<u>\$ 9,676,475</u>
Common stock issued for services	-	-	5,298,154	5,198	1,016,543			1,021,741		1,021,741
Non-controlling interest	-			-	-	-		-	(102,195)	(102,195)
Prior Period Adjustment	-			-	-		(1,676,383)	(1,676,383)		(1,676,383)
Net income attributable to Parent	-			-	-	-	3,166,130	3,166,130	-	3,166,130
Balances, December 31, 2011	<u>100,001</u>	<u>\$ 1,000</u>	<u>74,744,487</u>	<u>74,645</u>	<u>7,234,180</u>	<u>(133,336)</u>	<u>2,101,612</u>	<u>9,278,102</u>	<u>2,807,666</u>	<u>12,085,768</u>

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

ALLIED ENERGY, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
For the years ended December 31,
(UNAUDITED)

	2011	2010
Cash flows from operating activities:		
Net income	\$ 3,166,129	\$ (305,676)
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	551,262	559,477
Amortization of lease mineral rights	1,090,992	1,090,991
Stock compensation	1,021,741	856,935
Gain on disposal of fixed assets	(32,729)	(1,451)
Gain on sale of equity securities	-	(3,591)
Allowance for doubtful accounts	49,444	-
Impairment of drilling program sponsorships	1,356,464	-
impairment of investments	236,001	126,993
Deffered Comp underfunding		
Previous Period adjustment to LMR exp in Q1	1,668,113	
Net loss attributable to non-controlling stockholders	(102,195)	(19,834)
Changes in operating assets and liabilities:		
Prepaid expenses and other current assets	240,697	32,888
Employee loans	132,284	45,826
Deferred Income Tax asset	(598,091)	(234,848)
Inventory	23,386	(45,817)
Joint interest billing - in progress	(3,647,295)	(117,197)
Accounts receivable	(748,537)	767,620
Prefunding of drilling escrow account		(577,470)
Deferred compensation	(469,649)	26,506
Deposits	11,930	(4,745)
Other assets	(271,279)	
Accounts payable	(1,949,941)	2,958,494
Accrued liabilities	(26,738)	43,399
Accrued severance, net	(268,187)	947,558
Revenue Payable	341,367	323,928
Income tax payable	1,237,144	(72,956)
Deferred revenue	-	(376,776)
Deferred tax liability	260,265	(61,041)
	3,272,578	5,959,213
Cash flows from investing activities:		
Purchase of oil and gas properties	(1,784,296)	(2,837,326)
Purchase of investments in drilling program sponsorships	(24,488)	(80,485)
Purchase of investments	6,377	(90,000)
Purchase of property and equipment	(437,501)	(1,156,007)
	(2,239,908)	(4,163,818)
Cash flows from financing activities:		
Proceeds from note payable	729,247	530,633
Repayment of note payable	(1,226,000)	(528,818)
Proceeds from non-controlling stockholders		
Purchase of treasury stock	-	-
	(496,753)	1,815
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	535,917	1,797,210
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	3,406,298	1,609,087
CASH AND CASH EQUIVALENTS AT END OF PERIOD	\$ 3,942,216	\$ 3,406,297
Supplemental Disclosure of Cash Flows Information:		
Interest paid	\$ 75,215	\$ 154,521
Income taxes paid	\$	\$ 358,545
Supplemental Disclosure of non-cash investing and financing activities:		
Disposal of fully depreciated property and equipment	\$	\$ 177,299

See accompanying notes to the unaudited consolidated financial statements

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

ALLIED ENERGY, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
As of December 31, 2011

NOTE 1 – DESCRIPTION OF BUSINESS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Allied Syndications, Inc., d/b/a Allied Energy Group, Inc., was incorporated in Texas on June 3, 2003 to provide oil and gas services to investors. Technol Fuel Conditioners, Inc. (“Technol”) was incorporated in Colorado on March 6, 1998 as Interactive Golf Marketing Inc. Pursuant to a merger agreement between Technol and Allied Syndications, Inc. (“ASI”), in April 2005, all the outstanding shares of ASI’s common stock were exchanged for the common stock of Technol, and Technol was the surviving entity of the merger. Upon this transaction, the assets and all related debt of Technol, as Technol existed before the merger, were sold to former management, and post-merger Technol was released from all obligations and claims related to those assets. The resulting entity, Technol, was reincorporated in Florida and changed its name to Allied Energy Group, Inc. In December 2007, Allied Energy Group, Inc. changed its name to Allied Energy, Inc. (“Allied,” or the “Company”).

Allied is an independent oil and gas development company primarily engaged in the business of sponsoring and providing turnkey drilling and operations management services to oil and gas general partnerships sponsored by the Company. The Company’s subsidiary companies provide operating and maintenance services to the general partnerships. Allied’s strategic focus and goal is to develop oil and natural gas reserves for its sponsored partnerships, as well as for its own account. The partnerships sponsored by the Company are formed to develop oil and natural gas reserves in the continental United States. The Company may at times participate in the same prospects for its own account outside of the partnerships. Allied relies upon its industry partners and subcontracted well operators, as well as consulting geologists and petroleum engineers, and other operational personnel whose combined industry experience is essential to each project.

The Company’s majority-owned subsidiary, Allied Gas Transmission, Inc. (“AGT”), owns and operates a natural gas gathering and transmission line to service certain partnership wells in Rogers County, Oklahoma. In addition to AGT, Allied has two wholly-owned subsidiaries that act as operators for the sponsored general partnerships of the Company in Oklahoma and Texas, Allied Operating, LLC (“AO”), and Allied Operating Texas, LLC (“AOT”), respectively.

As of December 31, 2011, Allied was the managing general partner or general manager of 54 partnerships and joint ventures, with plans to establish and sponsor at least three additional partnerships during 2012. Allied holds small equity interests (generally less than 1%) in 20 of these partnerships, which include interests in an aggregate of 151 wells, including 108 producing wells.

As of December 31, 2011, in addition to the wells held by partnerships in which Allied has an interest, Allied owned varying small net revenue interests (generally less than 5%) in 7 wells that were producing or awaiting hook-up, and in 2 wells involved in testing or completion.

The consolidated financial statements include the accounts of Allied and its wholly-owned subsidiaries: Allied Operating, LLC (“AO”), Allied Alternative Energy, LLC (“AAE”), Allied Operating Texas, LLC (“AOT”) and Allied Holdings, LLC (“AH”), as well as the accounts of Allied Gas Transmission, Inc. (“AGT”), which is Allied’s 60%-owned subsidiary. Allied Energy, Inc. and its subsidiaries are collectively referred to as “Allied” or “the Company.” All significant inter-company transactions have been eliminated.

During February 2009, the Company established AGT to be in the business of constructing and managing gathering systems and/or pipelines related to some of the property interests owned by the Company’s partnerships. The Company owns 60% of AGT, and the remaining 40% is owned by outside stockholders. AGT currently owns approximately five miles of pipeline, giving several properties south of AGT’s main compression station access to gas purification, treatment and access to the high pressure line of the gas purchaser. In addition to its own facilities, AGT operates a leased amine unit to bring the raw gas to

ALLIED ENERGY, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
As of December 31, 2011

pipeline quality. AGT derives revenue from the transmission charges applied to existing wells owned by partnerships operated by Allied Energy or its subsidiaries. In addition, AGT has invested in the planning, engineering and possible acquisition and development of an approximately ten-mile natural gas transmission system to connect the Company's northern producing field in Oklahoma to the Company's southern lease in Oklahoma that includes a compressor station, master meter and tap. This system, if completed, would enable the Company to sell directly to the local purchaser and bypass the existing market to the North. Actual construction of this transmission system has not commenced. The economic feasibility of the plans to extend the current transmission lines to the North is currently being reviewed. No additional investments by AGT will be pursued until the review has been completed.

During December 2009, the Company established AH, which is engaged in the ownership and management of Allied's real estate holdings. As of December 31, 2011, these real estate holdings consisted of three properties, including the Company's office building. Each property is described more specifically below under Note 8 – Notes Payable.

During 2008, the Company established AAE to explore alternative energy sources. AAE never began operations and was dissolved in December 2011.

* * *

The following summarizes significant accounting policies to assist the reader in understanding and evaluating the consolidated financial statements. These policies are in conformity with accounting principles generally accepted in the United States of America (U.S. GAAP) and have been applied consistently in all material respects.

Use of Estimates– The preparation of financial statements in conformity with accounting principles in accordance with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, as well as certain financial statement disclosures. Although management believes that the estimates and assumptions used in the preparation of the consolidated financial statements are appropriate, actual results could differ from these estimates.

Concentration of Credit Risk – Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of cash and cash equivalents. The Company maintains cash balances with certain banks whose balances are insured by the Federal Deposit Insurance Corporation (“FDIC”) up to \$250,000. The FDIC's temporary Transaction Account Guarantee (“TAG”) Program provides depositors with unlimited coverage for non-interest-bearing transaction accounts at participating FDIC-insured institutions. All of the banks at which Allied maintains balances have elected to participate in the TAG Program. At various times throughout the year, the Company had amounts on deposit at financial institutions in excess of federally insurable limits.

Cash and Cash Equivalents– Cash and cash equivalents include cash on hand and cash in bank in interest-bearing and non-interest bearing accounts. Highly liquid investments with original maturities of three months or less are considered cash equivalents.

Allowance for Doubtful Accounts – The Company has elected to record bad debts using the allowance method. The estimated allowance is based upon historical data and other pertinent information relative to the receivables in question. Allied books receivables primarily to recognize investment monies called down from Allied's investment partnerships not yet received. Management expects this balance to remain low due to the nature of the financial commitment in which our partners have engaged. There was no such allowance recorded as of December 31, 2011 or December 31, 2010.

ALLIED ENERGY, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
As of December 31, 2011

Investments – The Company’s investment portfolio consists of an investment in equity securities, which are recorded at fair value and which are held as available for sale, and of long-term investments in a limited liability company and in general partnerships, which are recorded at cost and which are evaluated for other than temporary impairment on a quarterly basis in accordance with Accounting Standards Codification (“ASC”) 820, “Fair Value Measurements and Disclosures.” Investment in equity securities, which are held as available for sale, and the long-term investment in a limited liability company are included in the accompanying consolidated balance sheets as investments (See Note 4). Investments in general partnerships are included in the accompanying consolidated balance sheets as drilling program syndications and valued following the cost method (See Note 5).

The Company’s policy for the evaluation of securities to determine whether the impairment is other than temporary is based on analysis of the following factors: (1) rating downgrade or other credit event (e.g., failure to pay interest when due); (2) financial condition and near-term prospects of the issuer or non-issuer, including any specific events which may influence the operations of the issuer or non-issuer, such as changes in technology or discontinuance of a business segment; (3) prospects for the issuer’s or non-issuer’s industry segment; and (4) intent and ability of the Company to retain the investment for a period of time sufficient to allow for anticipated recovery in fair value. The Company evaluates its investments in securities to determine other than temporary impairment, no less than quarterly. Investments that are deemed other than temporarily impaired are written down to their estimated net fair value, and the related losses are recognized in operations.

Employee Loans – On a case-by-case basis, the Company has made non-interest bearing loans to employees. The balance of employee loans outstanding totaled \$77,175 and \$209,459, at December 31, 2011 and December 31, 2010, respectively.

Property and Equipment, Net– Property and equipment is recorded at cost, net of accumulated depreciation. Depreciation and amortization of property and equipment is computed using the straight-line method over the estimated useful lives of the related assets which range from five to thirty-nine years. Amortization of leasehold improvements is computed using the straight-line basis over the lesser of the estimated useful lives of the underlying assets or the terms of the related leases. When asset items are retired or otherwise disposed of, income is charged or credited for the difference between net book value and proceeds realized thereon. Ordinary maintenance and repairs are charged to expense as incurred. Replacements and Improvements to the property are capitalized.

Oil and Gas Properties – The Company uses the successful efforts method of accounting for oil and gas producing activities pursuant to the provisions of ASC 932, “Extractive Activities – Oil and Gas.” A significant portion of the Company’s oil and gas properties are controlled through leasing arrangements. Costs to obtain lands and acquire leased mineral rights with oil and gas properties, including costs to drill and equip exploratory wells that find proved reserves and to drill and equip development wells along with related asset retirement costs are capitalized. Costs to drill exploratory wells that do not find proved reserves, geological and geophysical costs, and costs of carrying and retaining unproved properties are expensed as incurred.

Unproved oil and gas properties that are individually significant are periodically assessed for impairment of value, and a loss is recognized at the time of impairment by providing an impairment allowance. Other unproved properties are amortized based on the Company’s experience of successful drilling and average holding period. Capitalized costs of producing oil and gas properties, after considering estimated residual salvage values, are depreciated and depleted in accordance with management’s best estimates.

Gains and losses are recognized on sales of entire interests in proved and unproved oil and gas properties. Sales of partial interests are generally treated as a recovery of costs and any resulting gain or loss is

ALLIED ENERGY, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
As of December 31, 2011

recorded as other income. The Company did sell partial working interests in certain producing wells during 2011. These transactions are appropriately reflected in the financial statements.

The Company records an impairment expense for suspended well costs, if the Company determines by assessing the reserves and economic viability of the project that the development of the well is not making sufficient progress.

Impairment of Long-lived Assets—In accordance with ASC 360-10, long-lived assets, such as property, plant and equipment, and oil and gas properties, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized for the amount by which the carrying amount of the asset exceeds the fair value of the asset.

Fair Value of Financial Instruments – The Company measures its financial assets and liabilities in accordance with U.S. GAAP. For certain financial instruments, including cash, accounts receivable, employee loans, accounts payable, accrued expenses and notes payable, the carrying amounts approximate fair value due to their short maturities.

Revenue Recognition – The Company recognizes revenue in accordance with ASC 605-10, “Revenue Recognition in Financial Statements.” Under these guidelines, revenue is recognized on sales transactions when all of the following exist: Persuasive evidence of an arrangement exists, delivery has occurred, the sales price is fixed or determinable and collectability is reasonably assured. The Company generates and recognizes revenue from the management of drilling program syndication partnerships, drilling and development of its own wells, transmission charges and consulting services it provides for drilling and development, when it has the contractual right to receive revenue.

The Company sells crude oil and natural gas under short-term agreements at prevailing market prices. The Company’s net revenue interest in the leased property is recognized at the point of sale, when the crude oil and natural gas is extracted from the tanks by the customer or purchaser, whereby the customer or purchaser has assumed the risks and rewards of ownership, the sales price is fixed or determinable and collectability is reasonably assured.

Stock-Based Compensation—The Company has adopted ASC 718-10, “Share Based Payment” and related interpretations. ASC 718-10 requires companies to estimate and recognize the fair value of stock-based awards to employees and directors. The value of the portion of an award that is ultimately expected to vest is recognized as an expense over the requisite service periods using the straight-line attribution method.

Advertising Costs— Advertising costs are charged to expense during the period in which they are incurred. Advertising expenses for the twelve months ended December 31, 2011 and 2010 approximated \$63,334 and \$63,400, respectively.

Income Taxes—The Company accounts for income taxes pursuant to the provisions of ASC 740-10, “Accounting for Income Taxes,” which requires, among other things, an asset and liability approach to calculating deferred income taxes. The asset and liability approach requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the carrying amounts and the tax bases of assets and liabilities. A valuation allowance is provided to offset any net deferred tax assets for which management believes it is more likely than not that the net deferred asset will not be realized.

ALLIED ENERGY, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
As of December 31, 2011

The Company has adopted the provisions of ASC 740-10, "Accounting for Uncertain Income Tax Positions." When tax returns are filed, it is highly certain that some positions taken would be sustained upon examination by the taxing authorities, while others are subject to uncertainty about the merits of the position taken or the amount of the position that would be ultimately sustained. In accordance with the guidance of ASC 740-10, the benefit of a tax position is recognized in the financial statements in the period during which, based on all available evidence, management believes it is more likely than not that the position will be sustained upon examination, including the resolution of appeals or litigation processes, if any. Tax positions taken are not offset or aggregated with other positions. Tax positions that meet the more-likely-than-not recognition threshold are measured as the largest amount of tax benefit that is more than 50 percent likely of being realized upon settlement with the applicable taxing authority. The portion of the benefits associated with tax positions taken that exceeds the amount measured as described above should be reflected as a liability for unrecognized tax benefits in the accompanying balance sheets along with any associated interest and penalties that would be payable to the taxing authorities upon examination. The Company believes its tax positions are all highly certain of being upheld upon examination. As such, the Company has not recorded a liability for unrecognized tax benefits. As of December 31, 2011, tax years 2006 through 2010 remain open for Internal Revenue Service ("IRS") audit. The Company has received no notice of audit from the IRS for any of the open tax years.

Allied and certain of its subsidiaries (AO, AAE, AOT and AH) file consolidated federal and applicable state income tax returns. AGT files separate federal and applicable state income tax returns, as Allied holds a 60% ownership interest in AGT.

The Company accrues for and remits income taxes on a pro-rata basis throughout the year based on the expected year-end liability. Estimates, judgments and assumptions are made quarterly based on available information and take into consideration estimated income taxes based on prior-year income tax returns, changes in income tax law, income tax strategies and other factors. In certain situations, revenue is remitted to the Company, when required by state laws, net of certain oil and gas related taxes.

Penalty/ Interest Policy – The Company's policy is to accrue penalties and interest on any required tax filings as well as uncertain tax positions, if any, in its consolidated statements of operations.

Legal Costs– In the normal course of business, the Company incurs costs to hire and retain external legal counsel to advise it on regulatory, litigation and other matters. The Company expenses these costs as the related services are received.

Environmental – The Company is subject to extensive federal, state and local environmental laws and regulations. These laws, which are constantly changing, regulate the discharge of materials into the environment and may require the Company to remove or mitigate the adverse environmental effects of disposal or release of petroleum, chemical and other substances at various sites. Environmental expenditures are expensed or capitalized depending on the future economic benefit. Expenditures that relate to an existing condition caused by past operations and that have no future economic benefit are expensed. Liabilities for expenditures of a non-capital nature are recorded when environmental assessment and/or remediation is probable and the costs can be reasonably estimated. As of December 31, 2011 and 2010, the Company has not recorded environmental remediation related costs and liabilities in the accompanying consolidated financial statements.

Earnings per Share – Basic earnings per share is computed in accordance with ASC 260-10, "Earnings Per Share," by dividing net income available to common shareholders by the weighted average number of common shares outstanding during the reporting period. Diluted earnings per share reflects the potential dilution that could occur if stock options and other commitments to issue common stock were exercised or equity awards vest resulting in the issuance of common stock that could share in the earnings of the Company. As of December 31, 2011, certain option agreements had been signed with board approval. As

ALLIED ENERGY, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
As of December 31, 2011

of December 31, 2011, there are both option agreements outstanding as well as commitments which may or may not be valid, enforceable or realized, some of which the Company intends to dispute. For the purposes of this disclosure, all potentially dilutive options and commitments have been taken into account for the calculation of earnings per share, even if the Company intends to dispute their validity.

Reclassification— Certain prior period amounts have been reclassified to conform to current period presentations.

Recent Accounting Pronouncements

In January 2010, the Financial Accounting Standards Board (“FASB”) published Accounting Standards Update (“ASU”) No. 2010-01 Equity (Topic 505) – “Accounting for Distributions to Shareholders with Components of Stock and Cash—a consensus of the FASB Emerging Issues Task Force,” as codified in ASC 505. ASU No. 2010-01 clarifies the treatment of certain distributions to shareholders that have both stock and cash components. The stock portion of such distributions is considered a share issuance that is reflected in earnings per share prospectively and is not a stock dividend. The amendments in this update are effective for interim and annual periods ending on or after December 15, 2009 and should be applied on a retrospective basis. Early adoption is permitted. The adoption of this standard did not have an impact on the Company’s consolidated financial position and results of operations.

In January 2010, the FASB published ASU No. 2010-02, “Consolidation (Topic 810) – Accounting and Reporting for Decreases in Ownership of a Subsidiary—a Scope Clarification,” as codified in ASC 810, “Consolidation.” This ASU clarifies the applicable scope of ASC 810 for a decrease in ownership in a subsidiary or an exchange of a group of assets that is a business or nonprofit activity. The ASU also requires expanded disclosures. The amendments in this update are effective for interim and annual periods ending on or after December 15, 2009, and should be applied on a retrospective basis. The adoption of this standard did not have an impact on the Company’s consolidated financial position and results of operations.

In January 2010, ASU No. 2010-3 was issued, which aligns the oil and gas reserve estimation and disclosure requirements of Extractive Industries – Oil and Gas (Topic 932) with the oil and gas reporting requirements of the U.S. Securities and Exchange Commission’s (“SEC”) Final Rule, “Modernization of Oil and Gas Reporting Requirements.” The SEC Final Rule, which was issued in December 2008, revised and expanded several disclosure requirements for public entities engaged in oil and gas producing activities. As stated in the adopting release of the SEC Final Rule, application was contingent on the FASB conforming its standards to the requirements of the SEC Final Rule. ASU 2010-3 is effective for annual periods ending on or after December 31, 2009 and is applied prospectively as a change in estimate. However, entities that became subject to the disclosure requirements of Topic 932 solely due to the change to the definition of significant oil and gas producing activities are permitted to apply the disclosure provisions of Topic 932 in annual periods beginning after December 31, 2009. The adoption of this standard did not have a material impact on the Company’s consolidated financial position and results of operations.

In January 2010, ASU No. 2010-06 “Fair Value Measurements and Disclosures (Topic 820): – Improving Disclosures about Fair Value Measurements” was issued. ASU No.2010-06 clarifies disclosure requirements related to fair value measurements and disclosures – Overall Subtopic (“Subtopic 820-10”) of the FASB Accounting Standards Codification. The new disclosures and clarifications of existing disclosures are effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosure about purchase, sales, issuances, and settlement in the roll forward of activity in Level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years. The amendments in this update are effective for interim and annual periods ending on or after December 15, 2009, and should be applied on a retrospective basis. The amendment did not have a material impact on the Company’s consolidated financial position

ALLIED ENERGY, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
As of December 31, 2011

and results of operations. The adoption of the disclosure requirement is not expected to have a material impact on the Company's consolidated financial position and results of operations.

In February 2010, the FASB issued ASU No. 2010-09 "Subsequent Events (Topic 855) Amendments to Certain Recognition and Disclosure Requirements." ASU No. 2010-09 requires that an SEC filer, as defined, evaluate subsequent events through the date that the financial statements are issued. The update also removed the requirement for an SEC filer to disclose the date through which subsequent events have been evaluated in originally issued and revised financial statements. The adoption of this guidance on January 1, 2010 did not have a material effect on the Company's consolidated financial statements.

In April 2010, the FASB issued ASU No. 2010-13 "Stock Compensation" (Topic 718). ASU No.2010-13 provides amendments to Topic 718 to clarify that an employee share-based payment award with an exercise price denominated in the currency of a market in which a substantial portion of the entity's equity securities trades should not be considered to contain a condition that is not a market, performance, or service condition. Therefore, an entity would not classify such an award as a liability if it otherwise qualifies as equity. The amendments in this update are effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2010. The amendments in this update should be applied by recording a cumulative-effect adjustment to the opening balance of retained earnings. The cumulative-effect adjustment should be calculated for all awards outstanding as of the beginning of the fiscal year in which the amendments are initially applied, as if the amendments had been applied consistently since the inception of the award. The cumulative-effect adjustment should be presented separately. Earlier application is permitted. The adoption of this guidance is not expected to have a material impact on the Company's consolidated financial statements.

In April 2010, the FASB issued ASU No.2010-14, "Accounting for Extractive Activities – Oil & Gas" (Topic 932). ASU No. 2010-14 amends FASB accounting Standard paragraph 932-10-S99-1 due to SEC Release No. 33-8995 [FR 78], "Modernization of Oil and Gas Reporting" and provides an update as to the amendments to SEC Regulation S-X, Rule 4-10. The adoption of this standard was effective in the second quarter of 2010 and did not have any impact on the Company's consolidated financial position and results of operations.

In April 2010, the FASB issued ASU No. 2010-17. "Revenue Recognition-Milestone Method" (Topic 605) ASU No.2010-17 provides guidance on defining a milestone and determining when it may be appropriate to apply the milestone method of revenue recognition for research or development transactions. An entity often recognizes these milestone payments as revenue in their entirety upon achieving a specific result from the research or development efforts. A vendor can recognize consideration that is contingent upon achievement of a milestone in its entirety as revenue in the period in which the milestone is achieved only if the milestone meets all criteria to be considered substantive. Determining whether a milestone is substantive is a matter of judgment made at the inception of the arrangement. The ASU is effective for fiscal years and interim periods within those fiscal years beginning on or after June 15, 2010. Early application is permitted. Entities can apply this guidance prospectively to milestones achieved after adoption. However, retrospective application to all prior periods is also permitted. The adoption of this guidance did not have a material impact on the Company's consolidated financial statements.

In August 2010, the FASB issued ASU No. 2010-21 (ASU No. 2010-21) "Accounting for Technical Amendments to Various SEC Rules and Schedules" and No. 2010-22 (ASU No. 2010-22) "Accounting for Various Topics – Technical Corrections to SEC Paragraphs." ASU No 2010-21 amends various SEC paragraphs pursuant to the issuance of Release No. 33-9026: "Technical Amendments to Rules, Forms, Schedules and Codification of Financial Reporting Policies." ASU No. 2010-22 amends various SEC paragraphs based on external comments received and the issuance of Staff Accounting Bulletin ("SAB") 112, "Business Combinations," which amends or rescinds portions of certain SAB topics. Both ASU No.

ALLIED ENERGY, INC. AND SUBSIDIARIES
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
 As of December 31, 2011

2010-21 and ASU No. 2010-22 were effective upon issuance. The amendments in ASU No. 2010-21 and No. 2010-22 did not have a material impact on the Company's consolidated financial statements.

Other ASUs not effective until after December 31, 2011, are not expected to have a significant effect on the Company's consolidated financial position or results of operations.

NOTE 2 – OIL AND GAS PROPERTIES, NET

Oil and gas properties include amounts incurred to acquire and develop leases and their related properties. The net balances as of December 31, 2011 and December 31, 2010 were \$2,061,675 and \$4,392,948, respectively. Lease Mineral Rights ("LMR") depletion and amortization expense was approximately \$1,090,992 for the twelve months ended December 31, 2011.

NOTE 3 – PROPERTY and EQUIPMENT, NET

	December 31, 2011	December 31, 2010
Furniture and fixtures - 7 yrs.	\$ 81,316	\$ 71,837
Equipment - 5 yrs.	958,819	873,228
Leasehold improvements– 7 yrs.	0	169,265
Building improvements– 7 yrs.	280,829	0
Automobiles – 5 year life	305,815	270,568
Property – 39 year life	465,740	465,740
Building – 39 year life	1,018,453	1,975,000
Gas transmission sys. – 22 yrs.	3,592,800	3,592,800
Sub-total	<u>6,703,772</u>	<u>7,418,438</u>
Less: acc. depreciation and amort.	<u>(1,282,504)</u>	<u>(883,409)</u>
Total	<u>\$ 5,421,268</u>	<u>\$ 6,535,029</u>

Depreciation and amortization expense was \$551,262 and \$559,477 for the twelve months ended December 31, 2011 and December 31, 2010, respectively.

NOTE 4 – INVESTMENTS

The Company had an investment in a limited liability company totaling \$236,201 as of December 31, 2010. In 2011, management carried out a review of the liquidity, cash flow, business development prospects and progress of the limited liability company. It concluded that the business no longer supported investment value and wrote the investment down to \$ 0 as of December 31, 2011. The Company's ownership of the long-term investment in this limited liability company ("LLC") did not exceed 20% of the LLC's equity and was recorded at cost considering the fact that the Company did not exercise significant influence over the LLC's management, financing and operating policies, and this investment did not qualify as in-substance common stock pursuant to the provisions of FASB ASC 323-10-15-13.

The Company had investments in equity securities of \$6,812 and \$12,989 for the twelve months ended December 31, 2011 and December 31, 2010, respectively. There was no significant change in our investment account during 2011. The investments are carried at fair value. Eventual gains or losses realized on short-term investment holdings are included in Other Income within the Consolidated Statement of Operations.

ALLIED ENERGY, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
As of December 31, 2011

NOTE 5 – INVESTMENTS IN DRILLING PROGRAM SYNDICATIONS

The Company acts as the managing general partner or general manager for several general partnerships for drilling program syndications. In general, the Company does not invest in these partnerships, although it may do so on occasion and/or it may receive a carried interest. As of December 31, 2011, none of the Company's interests in a partnership exceeded 3% of the partnership. Therefore, these investments are recorded at cost. As of December 31, 2011, there were no impairment charges recorded on drilling program syndications.

NOTE 6 – DEFERRED COMPENSATION PLAN

The Company maintains a deferred compensation plan (known as the "Executive Nonqualified Excess Plan") in the form of a Rabbi Trust, covering key executives of the Company as determined by the Board of Directors. The Rabbi Trust gives certain senior employees the ability to defer all or a portion of their salaries and bonuses to marketable securities that can be bought and sold at the employee's discretion. Although the assets have been primarily comprised of trading securities carried at their fair value, in 2011 the assets represented the cash value of a life insurance policy. The assets of the Rabbi Trust are available to satisfy the claims of the Company's creditors in the event of bankruptcy or insolvency of the Company. Participants may make voluntary pre-tax contributions to the deferred compensation plan. In addition, the Company may make discretionary matching contributions to the plan. The Company's contributions vest ratably over three years. At December 31, 2011, all participants were vested in the Plan. The unvested contributions under the deferred compensation plan totaled \$0 and \$84,868 at December 31, 2011 and December 31, 2010, respectively, and are included in the accompanying consolidated balance sheets. As of December 31, 2011, the Company had recorded a Company asset (represented by the cash value of a life insurance policy) of approximately \$ 554,417 and liabilities under deferred compensation plan of approximately \$ 626,083 of vested balances in favor of certain executives.

Effective as of January 9, 2012, the Company's deferred compensation plan was terminated.

NOTE 7 – 401(k) PROFIT SHARING PLAN

The Company has a 401(k) Plan ("Plan") to provide retirement and incidental benefits to its employees. Employees may contribute from 1% to 50% of their annual compensation to the Plan, limited to a maximum annual amount as set periodically by the IRS. The Company matches employee contributions dollar-for-dollar per person. All matching contributions vest to participants ratably over a six-year period, beginning with the second year of participation. The Company recorded contributions to the Plan of approximately \$56,835 and \$103,800 for the twelve months ended December 31, 2011 and 2010, respectively.

Effective as of October 1, 2011, the Company's 401K plan was terminated.

NOTE 8 – NOTES PAYABLE

In February 2011, the Company's home office building was sold to an independent third party, resulting in the Company's 50% acquisition as tenant-in-common being dissolved. The Company's five promissory notes in the aggregate face amount of \$1,750,000, which the Company had issued as part of the purchase price for its interest in the building, were waived by the holder of the note as part of the consideration received by the Company for its interest in the building. The holder of the note also returned to the Company all previous promissory note payments, totaling \$500,000, plus accumulated equity of approximately \$24,000, which was recorded as Other Income on the Consolidated Statement of Operations.

ALLIED ENERGY, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
As of December 31, 2011

On February 11, 2011 the Company purchased an 11,200 square foot building at 2427 Russellville Road in Bowling Green, Kentucky, for \$885,000. The building serves as the Company's new corporate headquarters. The building was financed through a financial institution with 20% down and the remaining \$708,000 financed by a promissory note. The promissory note is to be paid in monthly installments of \$5,878.11 for 180 months, at an interest rate of 5.75%. The note has an outstanding balance of approximately \$682,474 at December 31, 2011.

In August 2009, the Company acquired a truck for \$50,758 which was financed through a promissory note to a financial institution. The promissory note is payable in monthly installments of approximately \$1,180 for 48 months at an interest rate of 5.5% per annum and is collateralized by the truck. The Company has an outstanding balance of approximately \$22,530 and \$35,070 under this note at December 31, 2011 and December 31, 2010, respectively.

In August 2009, the Company acquired a truck for \$30,050 which was financed through a promissory note to a financial institution. The promissory note is payable in monthly installments of approximately \$935 for 36 months at an interest rate of 7.5% per annum and is collateralized by the truck. The Company has an outstanding balance of approximately \$7,294 and \$17,533 under this note at December 31, 2011 and December 31, 2010, respectively.

In May 2009, the Company acquired a truck for \$35,000 which was financed through a promissory note to a financial institution. The promissory note is payable in monthly installments of approximately \$1,577 for 24 months at an interest rate of 7.5% per annum and is collateralized by the truck. The Company paid off the note and has no outstanding balance at December 31, 2011.

In June 2010, the Company acquired a truck for approximately \$47,000, which was financed through a promissory note to a financial institution. The promissory note is payable in monthly installments of approximately \$1,100 for 48 months at an interest rate of 5.25% per annum and is collateralized by the truck. The Company has an outstanding balance of approximately \$30,448 and \$41,553 under this obligation at December 31, 2011 and December 31, 2010, respectively.

In October 2010, Allied Holdings, LLC purchased an investment property (land) for \$125,000. Allied Holdings, LLC made a down payment of \$18,750 for the property and obtained a \$106,250 loan through a promissory note to a financial institution. The promissory note is payable in monthly installments for 180 months at a variable interest rate of prime plus 300 basis points and is collateralized by the investment property. The monthly payment is approximately \$915. The Company had an outstanding balance of approximately \$101,074 and \$105,536 at December 31, 2011 and December 31, 2010, respectively.

In November 2010, Allied Holdings, LLC acquired 292 acres in Butler County, KY for \$372,592, with the intent to develop the oil and/or natural gas resources on the property. The property was financed through a promissory note to a financial institution. The promissory note is payable in monthly payments of \$3,194 for 180 months at an interest rate of 6.25%. The Company had an outstanding balance of approximately \$355,754 and \$371,312 at December 31, 2011 and December 31, 2010, respectively.

In July 2011, the Company acquired a Jeep Wrangler for approximately \$21,247, which was financed through a promissory note to a financial institution. The promissory note is payable in monthly installments of approximately \$646 for 36 months at an interest rate of 5% per annum and is collateralized by the vehicle. The Company has an outstanding balance of approximately \$18,523 at December 31, 2011.

Principal maturities of notes payable at December 31, 2011 are as follows:

ALLIED ENERGY, INC. AND SUBSIDIARIES
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
 As of December 31, 2011

Year	Amount
2012	\$ 89,702
2013	85,242
2014	72,187
2015	64,020
2016	67,934
Thereafter	839,014
	\$ 1,218,099

NOTE 9 – FAIR VALUE MEASUREMENTS

The Company records fair value of monetary and non-monetary instruments in accordance with ASC 820 “Fair Value Measurements and Disclosures.” The ASC establishes a framework for measuring fair value, establishes a fair value hierarchy based on inputs used to measure fair value, and expands disclosure about fair value measurements. Adopting this statement has not had a significant effect on the Company’s consolidated financial condition, cash flows, or results of operations.

In accordance with ASC 820, the financial instruments have been categorized, based on the degree of subjectivity inherent in the valuation technique, into a fair value hierarchy of three levels, as follows:

- Level 1: Inputs are unadjusted quoted prices in active markets for identical instruments at the measurement date (e.g., U.S. Government securities, publicly traded equity securities).
- Level 2: Inputs (other than quoted prices included within Level 1) that are observable for the instrument either directly or indirectly (e.g., certain corporate and municipal bonds and certain preferred stocks). This includes: (i) quoted prices for similar instruments in active markets, (ii) quoted prices for identical or similar instruments in markets that are not active, (iii) inputs other than quoted prices that are observable for the instruments, and (iv) inputs that are derived principally from or corroborated by observable market data by correlation or other means.
- Level 3: Inputs that are unobservable. Unobservable inputs reflect the reporting entity’s subjective evaluation about the assumptions market participants would use in pricing the financial instrument (e.g., certain structured securities and privately held investments).

ALLIED ENERGY, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
As of December 31, 2011

The composition of investments portfolio as of December 31, 2011 was as follows:

Investments	Level 1 Fair Value	Level 2 Fair Value	Level 3 Fair Value	Total Fair Value	Cost
Equity securities	\$ 6,812	\$ -	\$ -	\$ 6,812	\$ 9,399
Investment in limited liability company	-	-	0	0	500,000
Total Investments	<u>\$ 6,812</u>	<u>\$ -</u>	<u>\$ 0</u>	<u>\$ 6,812</u>	<u>\$ 509,399</u>
Investment in general partnerships (See Note 5)	-	-	230,034	230,034	322,643
Total Drilling Program Syndications	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 230,034</u>	<u>\$ 230,034</u>	<u>\$ 322,643</u>

The composition of investments portfolio as of December 31, 2010 was as follows:

Investments	Level 1 Fair Value	Level 2 Fair Value	Level 3 Fair Value	Total Fair Value	Cost
Equity securities	\$ 12,989	\$ -	\$ -	\$ 12,989	\$ 9,399
Investment in limited liability company	-	-	236,201	236,201	500,000
Total Investments	<u>\$ 12,989</u>	<u>\$ -</u>	<u>\$ 236,201</u>	<u>\$ 249,190</u>	<u>\$ 509,399</u>
Investment in general partnerships (See Note 5)	-	-	205,546	205,546	322,643
Total Drilling Program Syndications	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 205,546</u>	<u>\$ 205,546</u>	<u>\$ 322,643</u>

The Company's portfolio valuations classified as Level 3 are priced using subjective evaluation about the assumptions market participants would use in pricing the financial instrument, as well as using the annual financial statements of respective investees. The carrying value of Level 3 investments approximates the fair value at December 31, 2011. During the quarter, the Company recorded no impairments on

ALLIED ENERGY, INC. AND SUBSIDIARIES
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
 As of December 31, 2011

investments. Based on the criteria described above, the Company believes that the current level classifications are appropriate based on the valuation techniques used and that the fair values accurately reflect current market assumptions in the aggregate.

NOTE 10 – EQUITY

Capitalization

The Company has the following classes of stock authorized:

<u>Class</u>	<u>Par Value</u>	<u>Shares</u>
Common Stock	\$ 0.001	200,000,000
Preferred Stock	\$ 0.01	10,000,000

Common Stock

On September 18, 2008, the Board of Directors approved restricted stock grants totaling 5,804,375 common shares to three current and one former executive officer. The market price for the stock on that date was \$0.13 per share. Stock certificates representing the shares were issued in March of 2010.

In August 28, 2008, 350,000 restricted common shares were granted to the owners of United Producers as part of the acquisition of certain assets from United Producers by Allied Operating, LLC. Stock certificates representing the shares were issued in January of 2010.

During 2009, the Company issued 25,000 restricted shares of common stock for a total value of \$500 for services rendered.

On September 14, 2009 the Company agreed to grant to Hayden Energy Inc. options to purchase an aggregate of 6,198,541 common shares of the Company's authorized unissued share capital in accordance with various terms of the agreements between the Company and Hayden Energy Inc.

In June 2010, the Company issued 1,000,000 shares of restricted common stock to Hayden Energy Inc., valued at a total of \$95,000, for services performed during the acquisition of a working interest in an initial test well/unit located in Grimes County, Texas pursuant to the provisions of an agreement between Allied and Hayden Energy Inc.

In November 2010, 285,417 restricted common shares were issued as part of compensation to non-employee Directors for the years served from 2008 through 2010. The shares were valued at \$45,667.

In January 2011, the Board of Directors granted options to two Allied Energy executives for the purchase an aggregate of 2,000,000 restricted common shares at an exercise price of \$.01 per share and an expiration date of January 1, 2021, and in accordance with various other terms of the agreement. These grants are being reviewed for validity, legality, etc. as described below.

In February 2011, the Board of Directors issued 100,000 restricted common shares, valued at \$28,000, to a director in exchange for professional services to the Company.

In June 2011, the Company issued 5,198,154 common shares pursuant to exercise of stock options by Hayden Energy Inc. The shares issued were valued at approximately \$988,000.

ALLIED ENERGY, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
As of December 31, 2011

In June 2011, the Board of Directors began a review of certain prior issuances of stock and of stock options to directors and/or executive officers to determine the legality, validity and other justification of such transactions. Included in this review are the issuance of a total of 2,000,000 stock options to two executive officers in January 2011, and the issuance of 12,002,916 shares to executive officers, directors and certain other persons, in the years 2009, 2010, and 2011. This review has not been completed.

Preferred Stock

The Company has a class of 10,000,000 shares of preferred stock, issuable from time to time in one or more series. The board of directors is authorized to fix the dividend rights, dividend rate, conversion rights, voting rights, terms of redemption, preferences, restrictions and other matters relating to each series of preferred stock.

During 2008 the Company issued an aggregate of 100,000 shares of Series A preferred stock, valued at \$1,000, to the members of the executive management team. Each share of the Series A preferred stock has 1,000 votes on all matters presented to be voted upon by the holders of common stock. One share of Series A preferred stock has the same dividend and liquidation rights as one share of common stock so that the Series A preferred stock is pari passu with the common stock with respect to dividends and liquidation.

NOTE 11 – NON-CONTROLLING INTERESTS

During February 2009, Allied established AGT and issued 5,000,000 shares of common stock. Three million of these shares were issued to Allied, and two million, or 40%, were sold to investors who are not affiliates of Allied. The following is a reconciliation of the carrying amounts of total equity and the amounts attributable to Allied, which is referred to as the Parent, and to the non-affiliated stockholders (“Non-controlling Interest”):

	Parent	Non- controlling Interest	Total
Balances, December 31, 2010	\$ 557,792	\$ 2,909,862	\$ 3,467,654
Net Loss	(153,293)	(102,197)	(255,490)
Balances, December 31, 2011	<u>\$ 404,499</u>	<u>\$ 2,807,665</u>	<u>\$ 3,212,164</u>

Investment of Allied in AGT of \$404,499 is eliminated in consolidation.

NOTE 12 – COMMITMENTS AND CONTINGENCIES

Commitments

The Company leases office space, equipment and vehicles under various operating lease obligations with non-cancelable operating lease terms that expire at various dates through December 31, 2014. Certain operating lease agreements provide for an escalation clause, as applicable, to the base obligation. The Company is also responsible for certain operating expenses. The following is a schedule by year of the future minimum lease payments required under operating leases, which have initial or remaining non-cancelable terms in excess of one year as of December 31, 2011:

ALLIED ENERGY, INC. AND SUBSIDIARIES
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
 As of December 31, 2011

Years ending December 31,	Operating Leases
2012	\$ 85,186
2013	56,094
2014	14,623
2015	0
<u>Total minimum payments</u>	<u>\$ 155,903</u>

Drilling Commitments

The Company has given commitments to drill wells, on a turnkey basis, for seven sponsored general partnerships with aggregate expected costs of approximately \$ 9.0 million. The Company previously has received and recorded the turnkey revenue amounts received by the Company with respect to these commitments.

Contingencies

The Company has various lawsuits and claims arising in the ordinary course of its business. In the opinion of the Company, although final disposition of some or all of these suits and claims may impact the Company's consolidated financial statements in a particular period, they should not, in the aggregate, have a material adverse effect on the Company's consolidated financial position.

NOTE 13 – RELATED PARTY TRANSACTIONS

Employee Loans

The Company included amounts totaling \$77,175 and \$209,459 as employee loans receivable in the accompanying consolidated balance sheets at December 31, 2011 and at December 31, 2010, respectively. Amounts due represent unsecured non-interest bearing advances and do not follow any specific repayment terms.

NOTE 14 – SUBSEQUENT EVENTS

In October 2011, the Company, on behalf of one of its sponsored general partnerships, commenced drilling operations on the Rock Hill #1 prospect located on the Company's Wood County, Texas leasehold. The Company, as general manager of the partnerships, made a decision to relocate the drilling site to Wood County from the originally planned location on the Howard Lease in Grimes, County, Texas. Drilling activities were completed in November 2011, and in late January 2012, the Company determined to commence completion of the well. The Company owns a 24% cost-bearing working interest with an 18% net revenue interest, and an after-payout 9% working interest with a 6.75% net revenue interest in this well.

In November 2011, the Company signed contracts for the construction of an Amine Plant to purify the gas of two gas-producing wells in Grimes County, Texas, which were shut-in in most of December 2011. Construction and installation commenced at the end of November and was completed by December 14, 2011. Both gas wells are expected to resume production at approximately their previous rates. The Company is the general manager of the partnerships that own an interest in those wells. The Company owns a 16% working interest, with less than 1% net revenue interest in one of the wells, and a 13.4% working interest, with a 2.54% net revenue interest in the other well.

In November 2011, on behalf of one of its sponsored general partnerships, the Company commenced, drilling operations on the Champion Ranch #1H prospect located in Leon County, Texas. The Company directly owns a 25% cost-bearing billing interest with a 4.69% net revenue interest in this well. It also

ALLIED ENERGY, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
As of December 31, 2011

owns an interest in a partnership that it sponsored and formed for the purpose of drilling the Champion Ranch #1H prospect. The Company's interest in this partnership equates to an indirect 0.347% working interest and a 0.267% net revenue interest in the well.