U.S. ENERGY CORP.

ON TRACK

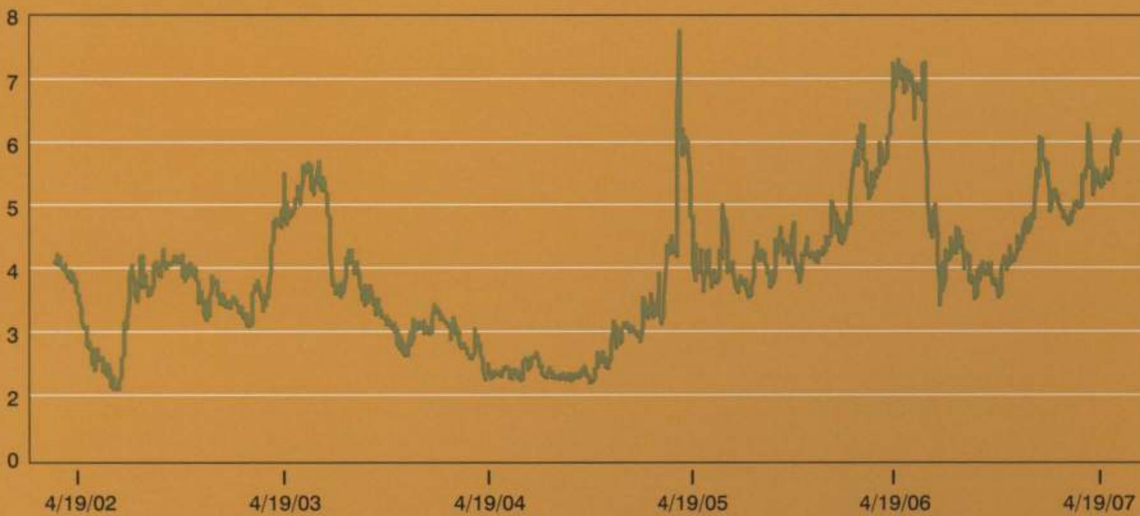
U.S. ENERGY CORP.
ANNUAL REPORT 2006

U.S. Energy Corp.

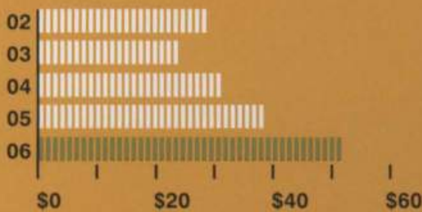
U.S. Energy Corp. is a diversified natural resource company with interests in uranium, molybdenum and gold.

U.S. Energy Corp.'s objective is to capitalize on the tremendous opportunities in the commodities markets today and transition to a positive cash flow entity. U.S. Energy Corp. is listed on the Nasdaq Capital Market under the symbol "USEG."

FIVE YEAR STOCK PRICING



TOTAL ASSETS
(IN MILLIONS)



CURRENT ASSETS
(IN MILLIONS)

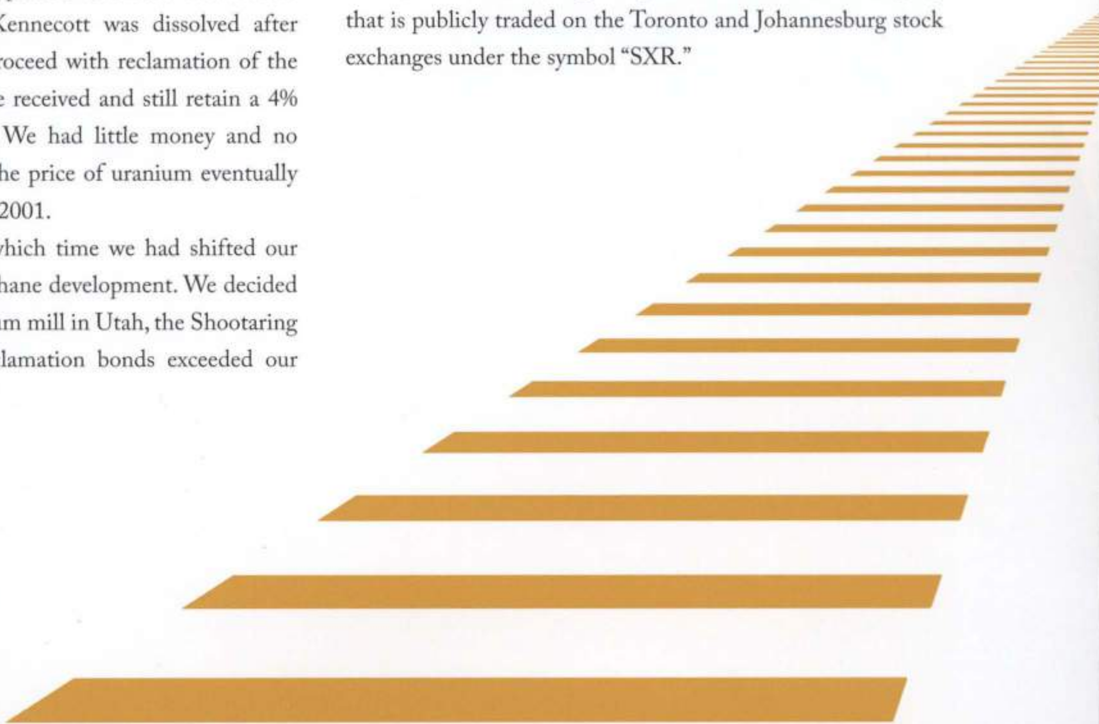
SHAREHOLDER'S EQUITY
(IN MILLIONS)

FORWARD THINKING

Dear Fellow Shareholders:

As I am writing this letter, your Company is preparing to close the largest transaction in its corporate history — the sale of the majority of its uranium assets to sxr Uranium One. The journey to this milestone has been a long one that dates back to my childhood. Along with my father Jack, my brothers and I began staking mineral claims at an early age. We staked Green Mountain in Wyoming when I was ten years old. We sold the Green Mountain uranium claims to Sinclair Oil & Gas (which later became ARCO) in 1970, and the claims were subsequently returned to us by ARCO when uranium prices collapsed in the mid eighties. We didn't stop there though. In 1990, my father sold the claims to Kennecott, which proceeded to spend nearly \$50 million to advance the Jackpot Uranium Mine and the Sweetwater Uranium Mill towards production. Things were great. The mine was advancing, the price of uranium was rising (to \$16.50/lb.), and we were expanding our uranium holdings in Utah with the acquisition of the Shootaring Canyon Mill and nearby mines. But then something unexpected happened. In 1997, the U.S. Government conveyed 72 millions pounds of stockpiled uranium to the newly formed U.S. Enrichment Corp. (USEC) to facilitate the sale of the government-owned enrichment facilities to USEC. Shortly thereafter, USEC announced plans to liquidate the material, and this caused the price of uranium to tumble to new lows within a short period of time. Both our Wyoming and Utah projects came to a standstill. Years of planning and permitting, along with tens of millions of dollars invested, suddenly appeared worthless. Within two years, our partnership with Kennecott was dissolved after the mining giant decided to proceed with reclamation of the Wyoming project (although we received and still retain a 4% royalty on Green Mountain). We had little money and no cash flow from operations as the price of uranium eventually skidded to \$6.40 per pound by 2001.

Fast forward to 2003, by which time we had shifted our corporate focus to coalbed methane development. We decided to reclaim our remaining uranium mill in Utah, the Shootaring Canyon Mill, as the cash reclamation bonds exceeded our estimate of reclamation costs. At this time, we requested an amendment in our license from "operational" to "reclamation" and by mid-2005, our amendment was granted. However, activity was picking up in the uranium market, once again, and the sale of our Rocky Mountain Gas (RMG) subsidiary in June 2005 provided U.S. Energy with another opportunity to realize the value of its uranium assets. The uranium price was moving higher and by July 2005 it had reached \$29.50 per pound. Could we actually realize significant value from assets that appeared worthless just a few years earlier? We believed so. In June 2005, we commissioned a study by Behre Dolbear (BD) to establish a "replacement value" for our uranium mill. The figure came back at \$80.5 million. However, BD also determined that it would cost us nearly \$40 million to re-start the mill, and we estimated that a similar amount would be required to resume production from nearby uranium mines, bringing the total required investment to nearly \$80 million. At that time, our shares were trading in the \$3.50 – \$4.50 per share range and the investment community turned a blind eye towards the value of our mill. They were more interested in "pounds in the ground." Canadian junior mining companies sprang up all around us, announcing pounds, and the market loved it. Meanwhile, unable to announce pounds utilizing the Canadian NI43-101 resource estimates, we set out to find a partner. We were confident in our ability to identify a "real" company (amongst hundreds) that would recognize the value of our mill, because mined uranium ore is worthless without access to a mill. Then we found sxr Uranium One (Uranium One), a globally diversified uranium company that is publicly traded on the Toronto and Johannesburg stock exchanges under the symbol "SXR."



REFLECTING ON SUCCESS

Our experienced people and diligent understanding of the markets we're involved with have led us to a track record of successful and profitable deals.

On April 30, 2007, we are scheduled to close the sale of the majority of our uranium assets to Uranium One for the following consideration:

- $750,000 cash (paid in advance on July 13, 2006);
- 6,607,605 sxr Uranium One common shares, currently valued at approximately $100 million (US) on April 25, 2007;
- A cash payment of $5,021,000, in accordance with a revised agreement between U.S. Energy Corp., Crested Corp., and Uranium Power Corp. ("UPC") that granted U.S. Energy Corp. and Crested Corp. the right to transfer all rights, responsibilities and obligations of certain UPC agreements, including the right to receive all payments thereunder ($3.1 million cash plus 1.5 million UPC common shares); and
- $1,585,000 cash to reimburse U.S. Energy Corp. and Crested Corp. for certain expenditures from July 10, 2006 to April 25, 2007.

Additional consideration, if and when certain events occur, will include:

- $20 million cash when commercial production occurs at the Shootaring Canyon Uranium Mill;
- $7.5 million cash on the first delivery to the Shootaring Canyon Mill following commercial production of mineralized material from any of the claims sold to sxr Uranium One; and
- From and after the date that commercial production occurs at the Shootaring Canyon Mill, a 5% production payment royalty up to but not more than $12.5 million.

JOHN L. "JACK" LARSEN

October 20, 1931 – September 4, 2006

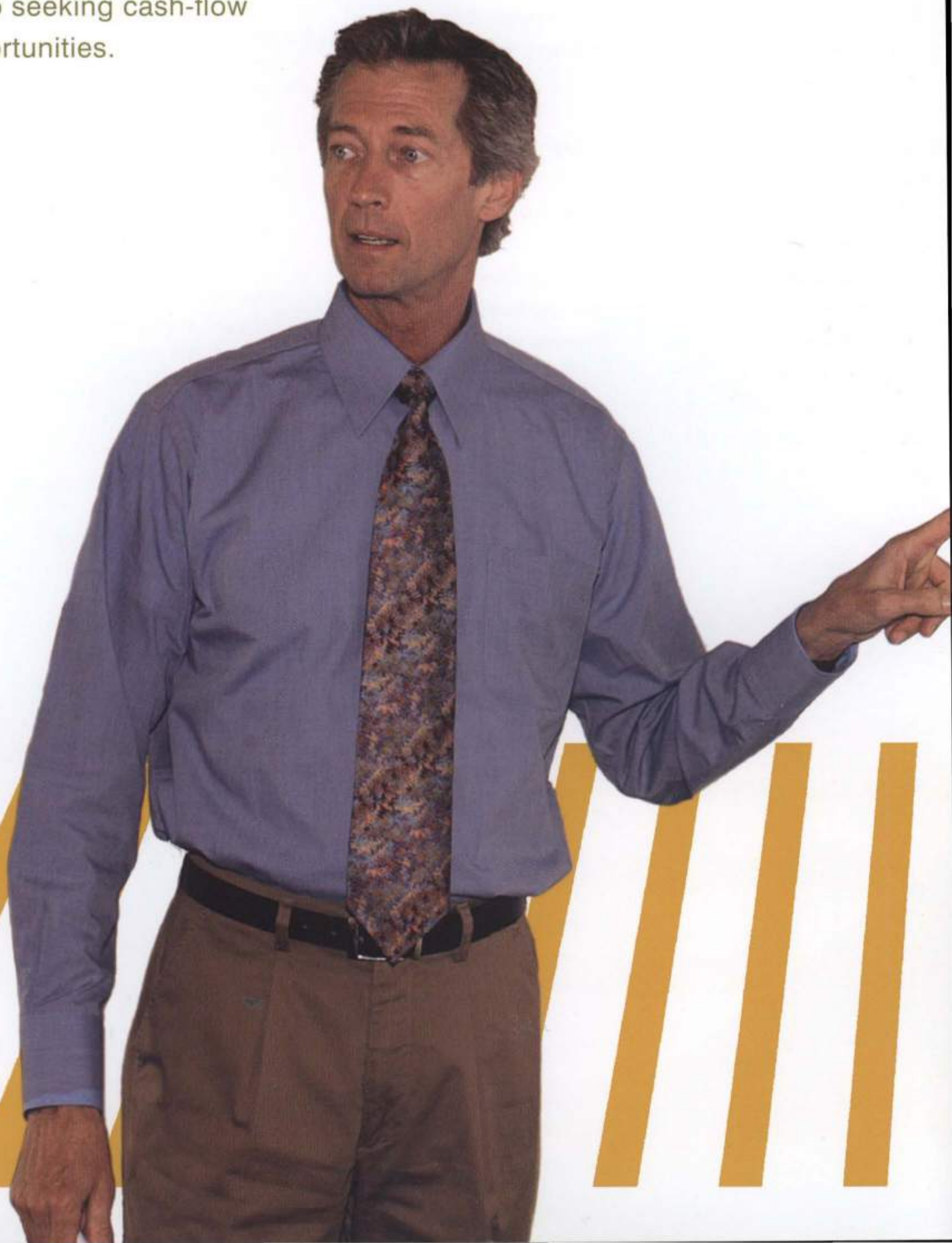
The year 2006 was a monumental year for U.S. Energy Corp., but it was also bitter sweet. On September 4, 2006 our founder, leader, friend and Dad said "See you later" his final time.

Jack was a visionary and this Company would not be what it is without his work ethic and tenacity. Over the years, Jack mined underground, swept walks, staked claims, took care of accounting, ran equipment, bought and sold properties, sought out partners, closed deals and "ran" this Company. He did all this with a sparkle in his eye and a smile on his face. All those that knew Jack, knew that he was "one of a kind." He was extremely proud to be a Wyoming resident and told all whom he met, with that same sparkle in his eyes, that he was from Riverton, Wyoming, the "greatest place on earth."

If there is Uranium, Gold, Molybdenum or other minerals in heaven (and there surely is) then that's where you can find Jack today. Digging and dealing and laying the foundations so that we all have a better place when "we" get there. "Thanks" Jack – We'll miss you!

ADVANCING OUR EXPECTATION

We are prudently investing the Company's capital resources and will remain focused on the mineral sector while also seeking cash-flow investment opportunities.



MOVING FORWARD

of Sutton Resources, he was instrumental in the sale of that company's Tanzanian gold property to Barrick Gold for $525 million. In 2005, as Chairman of Caneco Resource Corp., he oversaw the sale of its nickel property to South American giant CVRD for $950 million. Additionally, as Chairman of Polaris Minerals Corp., Mr. Shklanka recently played a role in the permitting and the initiation of production at its $51 million aggregate operation on B.C. Island that ships product to its new $27 million Richmond Terminal in the San Francisco Bay. Mr. Shklanka has a record of achievements that make us proud to be associated with him and his team at Kobex.

Under the terms of our agreement, Kobex is responsible for the first $50 million in expenditures at the Lucky Jack Project. When its investment reaches $15 million, Kobex will earn a 15% interest in the project, and upon spending a total of $50 million at Mt. Emmons, it will earn a 50% interest in the project. At that time, we will decide whether to (1) continue the joint venture; (2) allow Kobex to earn another 15% equity interest (65% total) by providing all project financing; or (3) merge our operating company, U.S. Moly Corp. (or another wholly-owned entity) into Kobex.

We have a lot of work to do in the coming years at Lucky Jack and that work has begun in earnest. We plan to submit our Plan of Operations for the mine/mill complex to the U.S. Forest Service in the fourth quarter of 2007. Pursuant to this, we have already engaged consultants to work on the Plan of Operations as well as socioeconomic, transportation, hydrology, geotechnical and electrical studies. Additionally, we have approved an underground rehabilitation program for the existing mine workings that is anticipated to be followed by a comprehensive underground close-spaced core drilling program in the high grade section of the mine. Further, under the leadership of Clyde Gillespie, we have launched an intensive community relations program, begun work on several water treatment plant upgrades, and upgraded our existing safety program.

The Lucky Jack property was permitted once before — in 1980 — when AMAX owned the property. It was permitted for a 20,000 ton per day (tpd) operation that would have "block caved" the mine. AMAX, however, did not sign the permit due to depressed molybdenum prices. Today we are planning a smaller mine, and technology is our friend. Advances in technology in recent years should allow us to handle materials and waste much more effectively and efficiently while minimizing impacts to the environment.

I am very confident that Lucky Jack will be permitted in a timely fashion. Together with Kobex and the local communities, we plan to make the mine a "win-win" situation for all parties involved. We are eager to share our plans with the local citizens and to win their support with a community-compatible mine plan that will provide long-term jobs, revenue and tax base benefits, and a mine that we can all be proud of from an environmental perspective. Together, we will accomplish these goals.

Your Company also has a solid position in gold with its 55% equity position in Sutter Gold Mining Inc. (SGM), which trades on the Toronto Venture Exchange under the symbol "SGM. V." After securing all of the major permits required to move toward production at its Sutter Gold Project in the Mother

agreements with more strength than at any time in our history.

Further, while our primary focus will remain in the minerals development arena, we are also seeking cash-flow investment opportunities. One such opportunity that we are now exploring involves the construction of multifamily housing in the energy (mining and natural gas) basins of the intermountain west. We believe this represents an opportunity to create revenues and solid cash flows that are built around industries we are familiar with, namely mining and oil/gas production. Today, the intermountain west is experiencing unprecedented growth in Wyoming, Utah and Colorado, and these states will be our target markets.

The first multifamily project that we are considering is in Gillette, Wyoming. Gillette is expected to increase its population from 27,000 to 50,000 by the year 2015. Its growth reflects increases in coal production (440 million tons in 2006 in Wyoming, expected to reach 600 million tons by 2012) and coalbed methane production. The Powder River Basin in northeast Wyoming leads the state in both coal and gas production. Due to housing shortages, many companies have simply quit hiring as housing cannot be built on a timely basis. Additionally, three new coal-fired power plants are slated to start construction in the years 2007 through 2009, further exacerbating the housing shortage. Basin Electric expects to begin plant construction late this year and anticipates the hiring of 1,250 employees for the five-year project. Gillette is our first target market for many obvious reasons, and should we decide to build the project, we expect to pre-lease 80% of the 216-unit complex before construction begins. Similar opportunities are available throughout the intermountain west, and we plan to capitalize on such potential in the coming years.

We had an eventful and exciting year in 2006. We are in the process of realizing tremendous value from assets that a short time ago were considered of little or no value in the market price of our stock. Management stayed the course however, and our shareholders are now being rewarded for this vision.

In summary, I believe that we have set a course that has the potential to deliver outstanding value to our shareholders in future years. We have shifted the holding, operating and advancement costs of Lucky Jack to a dedicated joint venture partner. The outlook for our Lucky Jack Project is very promising, as molybdenum prices are expected to remain strong due to demand from emerging economies in China and India, and from the global energy industry. We believe our project outshines all others due to its size, potential ore grade, and our partnership with Kobex (which on April 26, 2007 announced a "bought" equity financing in excess of $20 million for the Lucky Jack Project).

U.S. Energy Corp.'s management is seeking to maximize opportunities in the natural resource sectors for the benefit of our shareholders.

Additionally, we are in the process of merging Crested to create greater market visibility, and we are looking to invest in revenue-generating activities with minimal workforce requirements. Lastly, we will continue to evaluate mineral investment opportunities that meet our entry criteria and offer extraordinary return-on-investment potential.

Building shareholder value is management's primary goal. The successful execution of our business plan, with an emphasis on natural resources and cash-flow-generating investments, represents our top priority in pursuit of this goal.

Thank you for your continued support of U.S. Energy Corp. I am honored to serve as your president and look forward to the further enhancement of your shareholder value in 2007 and beyond. We have an experienced, dedicated and cohesive management team and board of directors that are dedicated to this goal.

Mark J. Larsen
President/Chief Operating Officer
April 27, 2007

Selected Financial Data

The selected financial data is derived from and should be read with the financial statements included in this Report.

	December 31,				
	2006	2005	2004	2003	2002
Current assets	$ 43,325,200	$ 7,840,600	$ 5,421,500	$ 5,191,400	$ 4,755,300
Current liabilities	11,595,200	1,232,200	6,355,900	1,909,700	2,044,400
Working capital (deficit)	31,730,000	6,608,400	(934,400)	3,281,700	2,710,900
Total assets	51,901,400	38,106,700	30,703,700	23,929,700	28,190,600
Long-term obligations(1)	882,000	7,949,800	13,317,400	12,036,600	14,047,300
Shareholders' equity	32,977,400	24,558,200	6,281,300	6,760,800	8,501,600

(1)Includes $124,400, of accrued reclamation costs on properties at December 31, 2006, $5,669,000 December 31, 2005, $7,882,400 at December 31, 2004, $7,264,700 at December 31, 2003, and $8,906,800 at December 31, 2002. See Note K of Notes to Consolidated Financial Statements.

	Year Ended				Seven Months Ended
	December 31, 2006	December 31, 2005	December 31, 2004	December 31, 2003	December 31, 2002
Operating revenues	$ 813,400	$ 849,500	$ 815,600	$ 513,500	$ 673,000
Loss from continuing operations	(16,670,700)	(6,066,900)	(4,983,100)	(5,066,800)	(3,524,900)
Other income & expenses	2,302,700	(484,000)	465,100	(311,500)	(387,100)
(Loss) income before minority interest, equity in income (loss) of affiliates, income taxes, discontinued operations, and cumulative effect of accounting change	(14,368,000)	(6,550,900)	(4,518,000)	(5,378,300)	(3,912,000)

	December 31,	December 31,	December 31,	December 31,	Seven Months Ended December 31,
	Year Ended				
	2006	2005	2004	2003	2002
Minority interest in loss (income) of consolidated subsidiaries	--	--	0.02	0.00	--
Benefit income taxes	0.81	--	--	--	--
Discontinued operations, net of tax	--	0.94	(0.15)	(0.18)	--
Cumulative effect of accounting change	--	--	--	0.14	--
Preferred stock dividends	--	--	--	--	--
Net (loss) income per share, basic	$ 0.06	$ 0.55	$ (0.48)	$ (0.52)	$ (0.36)
Net (loss) income per share, diluted	$ 0.05	$ 0.55	$ (0.48)	$ (0.52)	$ (0.36)

Molybdenum - Annual Metal Week Dealer Oxide mean prices averaged $25.55 per pound in 2006 compared with $32.94 per pound in 2005, $16.41 per pound in 2004, $5.32 in 2003 and $3.77 in 2002. Continued strong demand has outpaced supply over the past several years (deficit market conditions) and has reduced inventory levels throughout the industry. At March 9, 2007, the price was $28.25 per pound.

The rebound in the above commodity prices present opportunities. The Company holds what we consider to be significant mineral and related properties in gold and uranium, and received a significant molybdenum property from Phelps Dodge Corporation ("PD") on February 28, 2006. In contrast to the prior five years, we now have cash on hand sufficient for general and administrative expenses, the continuation of our uranium property acquisition and exploration plan, and operation of the water treatment plant on the molybdenum property. Kobex Resources Ltd. is expected to pay the Lucky Jack molybdenum property permitting expenses and water treatment plan operating costs, and if the Uranium One contract is closed, additional cash will be available to acquire new mineral properties and pursue other business opportunities.

Management's strategy to generate a return on shareholder capital is first, to demonstrate prospective value in the mineral properties sufficient to support substantial investments by large industry partners and second, to structure these investments to bring capital and long term development expertise to move the properties into production. There are uncertainties associated with this strategy.

Forward Looking Statements

This Report includes "forward-looking statements" within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended ("the Exchange Act"). All statements other than statements of historical fact included in this Report are forward-looking statements. In addition, whenever words like "expect", "anticipate", or "believe" are used, we are making forward looking statements. Actual results may vary materially from the forward-looking statements and there is no assurance that the assumptions used will be realized in fact.

Critical Accounting Policies

Principles of Consolidation - The consolidated financial statements of USE and subsidiaries include the accounts of the Company, the accounts of its majority-owned or controlled subsidiaries Plateau (100%), Crested (70.9%), Four Nines Gold, Inc. ("FNG") (50.9%), Sutter Gold Mining Inc. ("SGMI") (49.6%), Yellow Stone Fuels, Inc. ("YSFI") (49.1%), and the USECC Joint Venture ("USECC"), a consolidated joint venture which is equally owned by USE and Crested, through which the bulk of their operations are conducted. Additional subsidiaries have been organized by the Company and include U.S. Moly Corp. ("USMC") for molybdenum and InterWest, Inc. ("InterWest") for real estate. The Company on a consolidated basis owns 90% of these subsidiaries with the remaining 10% being owned by employees, officers and directors of the Company.

Investments in joint ventures and 20% to 50% owned companies are accounted for using the equity method. Because of management control and debt to the Company which may be converted to equity, SGMI and YSFI are consolidated into the financial statements of the Company. Investments of less than 20% are accounted for by the cost method. All material inter-company profits, transactions and balances have been eliminated.

Marketable Securities - The Company accounts for its marketable securities (1) as trading, (2) available-for-sale or (3) held-to-maturity. Based on the Company's intent to sell the securities, its equity securities are reported as a trading security. 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.

Mineral Claims - We follow the full cost method of accounting for mineral properties. Accordingly, all costs associated with acquisition, development and capital equipment as well as construction of plant relating to mineral properties are capitalized and are subject to ceiling tests to ensure the carrying value does not exceed the fair market value. All associated general and administrative as well as exploration costs and expenses associated with mineral properties are expensed when incurred.

All capitalized costs of mineral properties subject to amortization and the estimated future costs to develop proved reserves, are amortized by applying the unit-of-production method using estimates of proved reserves. Investments in unproven properties and major construction and development projects are not amortized until proven reserves associated with the projects can be determined or until impairment occurs.

If the sum of estimated future cash flows on an undiscounted basis is less than the carrying amount of the related asset, an asset impairment is considered to exist. The related impairment loss is measured by comparing estimated future cash flows on a discounted basis to the carrying amount of the asset. Changes in significant assumptions underlying future cash flow estimates may have a material effect on the Company's financial position and results of operations. An uneconomic commodity market price, if sustained for an extended period of time, or an inability to obtain financing necessary to develop mineral interests, may result in asset impairment. If the results of an assessment indicate that the properties are impaired, the capitalized cost of the property is expensed.

Asset Impairments - We assess the impairment of property and equipment whenever events or circumstances indicate that the carrying value may not be recoverable.

Asset Retirement Obligations - The Company records the fair value of the reclamation liability on its shut down mining properties as of the date that the liability is incurred. The Company reviews the liability each quarter and determines if a change in estimate is required as well as accretes the total liability on a quarterly basis for the future liability. Final determinations are made during the fourth quarter of each year. The Company deducts any actual funds expended for reclamation during the quarter in which it occurs.

Assets and Liabilities Held for Sale – Long lived assets and liabilities that will be sold within one year of the financial statements are classified as current. At December 31, 2006 the Company believed that its uranium assets in Wyoming, Utah, Colorado and Arizona would be sold within a twelve month period. All capitalized asset balances associated with these assets, including cash bonds pledged as collateral for reclamation liabilities, were therefore classified as Assets Held for Sale as of December 31, 2006. Likewise all asset retirement obligations as well as any other liability associated with these properties was classified as current Liabilities Held for Sale at December 31, 2006. In the event that these assets and liabilities are not sold, they will be re-evaluated to insure that no impairment has taken place and re-classified as long term assets and liabilities.

Real Estate Held for Sale – The Company classifies Real Estate Held for Sale as assets that are not in production and management has made the decision to dispose of the assets.

The Company recorded a net loss before benefit from income taxes of $14,279,400, of which $8,608,500 consisted of non-cash transactions. The largest of these non-cash transactions were: depreciation, $510,900; accretion of asset retirement obligations relating to the Company's mining properties, $766,500; loss on the valuation of the Enterra Acquisition units of $3,845,800; loss on valuation of the imbedded derivative associated with the Enterra Acquisitions D shares, $630,900; non-cash compensation relating to the 2001 stock award plan, expensing of employee options, accrual of executive retirement benefits and the accrual of the Employee Stock Ownership Plan, $1,328,600, and the expense associated with the extension and revaluation of warrants and the issuance of common stock for the payment of services for a total non cash services expense of $1,525,800.

These non-cash costs and expenses for the twelve months ended December 31, 2006 were offset by a gain of $3,063,600 on the sale of assets and a gain on the sale of the equity interest in Pinnacle of $10,815,600. The sale of assets represents primarily the cash and stock receipts from Uranium Power Corp. ("UPC") for its payments toward the purchase of a 50% undivided interest in certain of our uranium properties.

During the year ended December 31, 2006, the Company received $8,304,300 from the sale of Enterra units; $13.8 million from the sale of the Pinnacle shares, $398,100 from the sale of the UPC shares and $60,300 from the sale of Dynasty shares which were shares of a non-affiliated company owned by SGMI. The Company also received $2,410,600 in proceeds from the sale of property and equipment. The cash proceeds from the sale of property and equipment relate primarily to the sale of miscellaneous equipment which was no longer needed and the cash received from UPC pursuant to its agreement. During the twelve months ended December 31, 2006, the Company purchased equipment to manage the Lucky Jack molybdenum property. The assets purchased consisted of a loader, vehicles and miscellaneous other smaller equipment. The net cash used in these purchases was $649,300. The acquisition and development drilling on mining claims during the year ended December 31, 2006 consumed $1.6 million. Of this amount $775,300 was expended by SGMI on its properties and the remainder was expended on the uranium properties which are subject to the sale of all the uranium assets to Uranium One.

Cash flows from financing activities were primarily as a result of the issuance of the Company's common stock as a result of the exercise of stock warrants and options, $1,020,300; the issuance of SGMI common stock in private placements, $3,413,800 and proceeds from long term debt of $297,300 for the financing of the purchase of equipment and the financing of liability insurance premiums. These sources of cash from financing activities were off set by payments made on long term debt in the amount of $457,800.

The Company believes that the current market prices for gold, uranium and molybdenum are at levels that warrant further exploration and development of the Company's mineral properties. Management of the Company anticipates these metals prices will remain at levels which will allow the properties to be produced economically. Management of the Company therefore believes that sufficient capital will be available to develop its mineral properties from strategic industry partners, debt financing, and the sale of equity or a combination of the three. Successful development and production of these properties could greatly enhance the liquidity and financial position of the Company.

Navigant Capital Advisors, LLC is acting as financial advisor to the Company's special committee, and Neidiger Tucker Bruner Inc. is acting as financial advisor to the Crested special committee. These firms have delivered opinions to the Company and Crested, to the effects that the exchange ratio is fair to the Company's shareholders and to the Crested minority shareholders, respectively.

Management believes that the merger of Crested into the Company will enhance shareholder value due to consolidation of assets, simplification of reporting requirements and the application of all resources to one company.

Capital Resources

Contract to Sell Uranium Assets to Uranium One and the UPC Agreement

On February 22, 2007, the Company signed an asset purchase agreement with sxr Uranium One Inc. ("Uranium One"), and certain of its private subsidiary companies. If this agreement is closed, Uranium One will buy all the uranium assets and take over the Company's rights in the UPC purchase and mining venture. These proceeds will substantially enhance liquidity, and with respect to UPC, the receipt of approximately $5 million from Uranium One for UPC's future obligations under its purchase agreement with the Company will eliminate the uncertainty associated with UPC making those payments under the UPC purchase agreement (UPC would be paying Uranium One following the closing of the asset purchase agreement).

Kobex Resources Ltd. Agreement

On October 6, 2006, the Company signed an agreement (amended December 7, 2006) giving Kobex Resources Ltd. ("KBX") an option to acquire up to a 65% interest in the Lucky Jack molybdenum property. The principal financial benefit to be realized in 2007 and thereafter by the Company of Kobex performance under the agreement, is that Kobex will fund substantial costs and expenses which otherwise may have to be funded by the Company (including paying for the water treatment plant, obtain necessary permits, and have performed a bankable feasibility study preparatory to mining or selling the property). See "Lucky Jack Molybdenum Property" below.

Sutter Gold

During the second quarter of 2006, SGMI raised $3,171,500 of net proceeds from two private placements of its common stock. SGMI also received and additional $242,300 from the exercise of options and warrants. Proceeds from these private placements were used to fund a combined underground and surface diamond drill program during 2006 and the first quarter of 2007. As of December 31, 2006 SGMI had $1,618,300 on hand. The results of the drilling program are still being reviewed and studied. If warranted, a feasibility study on the SGMI property, which is an advanced stage gold project in the historic Mother Lode district located about 50 miles southeast of Sacramento, California, will be conducted.

Line of Credit

The Company has a $500,000 line of credit with a commercial bank. The line of credit is secured by certain real estate holdings and equipment. This line of credit is used for short term working capital needs associated with operations. At December 31, 2006, the entire amount of $500,000 under the line of credit was available to the Company.

On October 6, 2006 the Company entered into an agreement with KBX to potentially pay the standby and water treatment costs associated with the Lucky Jack property. See discussion above under Capital Resources. Until such time as the Company is able to find an industry partner to participate in the Lucky Jack property it will be responsible for one half of the costs of holding the property which will be significant

Sutter Gold Mining Inc. Properties

SGMI initiated an 18,000 foot underground and surface drilling program during the second quarter 2006, to further delineate and define potential resources at the property. The 2006 drill program included both underground and surface holes. As of September 30, 2006, 15 out of the 24 planned underground step-out and infill drill holes have been completed, which represents approximately 3,000 feet of the overall 18,000 foot surface and underground drill program. On September 14, 2006, Sutter announced that it intersected three new mineralized zones plus significant extensions to four shoots hosting previously reported mineral resources. The 9 to 12 hole surface drill program is to grid test an area containing what may be another significant mineralized zone in the K5 Vein, historically mined on Sutter's property at the South Spring Hill Mine.

Capital to fund these projects was obtained from private placements of SGMI's common stock. See Capital Resources above. SGMI is seeking additional funding for its drilling operations as well as engineering and geologic studies which are needed to raise sufficient capital to place the property into production.

Debt Payments

Debt to non-related parties at December 31, 2006 was $1,232,100 of which $937,200 will become payable during the year ending December 31, 2007. The largest component of the current debt payable is related to one of the Company's aircraft. The balance of the debt consists of debt related to the purchase of vehicles, equipment and the financing of insurance policy premiums.

Reclamation Costs

The asset retirement obligation on the Plateau uranium mineral properties and the Shootaring mill in Utah at December 31, 2006 is $4,117,400. This liability is fully collateralized by restricted cash investments of $6,883,200. It is currently anticipated that the reclamation of the Plateau uranium mill will not commence until 2033.

The asset retirement obligation of the Sheep Mountain uranium properties in Wyoming at December 31, 2006 is $2,409,800 and is collateralized by a reclamation bond which is secured by a pledge of certain real estate assets of the Company and cash bonds in the amount of $575,000.

In the event that the proposed transaction with Uranium One is successfully closed, the asset retirement obligations associated with the Shootaring mill and the Sheep Mountain uranium properties will be assumed by Uranium One. As a result of the assumption of those asset retirement obligations, the government agencies which hold various assets pledged against these obligations, would return those assets to the Company. Specifically, the pledge of the Company's corporate headquarters office building would be released and the building would be owned free and clear of any debt or obligation, and the $6.8 million cash bond pledged for the Shootaring Canyon Mill would be released to the Company. The release of these assets to the Company is dependent on the closing of the transaction with Uranium One.

Year Ended December 31, 2006 Compared with the Year Ended December 31, 2005

Operating revenues were reduced by $36,100 to $813,400 at December 31, 2006 from $849,500 at December 31, 2005. Components of this reduction of revenues were reductions in real estate operations of $68,300 which was offset by an increase in management fees of $32,200. Revenues from real estate operations decreased primarily as a result of the Company selling one of its office buildings which was no longer needed. Management fees increased due to billable services under the Uranium One and KBX agreements. Mineral property holding costs increased by $936,500 during the year ended December 31, 2006 to $2,312,800 as compared to $1,376,300 during the year ended December 31, 2005. The increase in mineral property holding costs is due to the increased geological and engineering activity on the Company's mineral properties and the holding costs associated with the Lucky Jack molybdenum property and associated water treatment plant. The water treatment plant and other Lucky Jack property costs were approximately $125,000 per month. These costs will now be paid by KBX as their capital contributions under the agreement. If the KBX transaction does not continue, the Company will remain responsible for these holding costs.

General and Administrative expenses increased by $7,064,000 during the year ended December 31, 2006 over those recorded during the prior year. This increase in General and Administrative expenses is as a result of (1) the payment of a $3 million bonus distributed amongst all employees of the Company (2) the settlement of other litigation, $395,000 (3) maintenance for the Company's airplane $353,700 (4) an increase of general and administration costs at Sutter of $302,000 due to the drilling program and associated increased number of employees as well as non-cash expenditures of: (a) the expensing of employee options pursuant to SFAS 123(R) which vested in 2006, $273,600; (b) accrual of the executive retirement benefits adopted in October 2005, $419,400, and (c) increased professional services paid for through the issuance of common stock and the extension of warrants, $347,900.

During the December 31, 2006, the Company recognized $3,063,600 from the sale of assets while during the year ended December 31, 2005 the Company recognized $1,311,200 from the sale of assets. This increase of $1,752,400 was primarily due to cash and common stock payments from UPC along with the sale of a no longer needed office building, $126,500, and the sale of miscellaneous equipment.

During calendar 2006, the Company recognized a non-cash loss of $630,900 from the valuation of the imbedded derivative associated with the Acquisitions Class D shares discussed above under Capital Resources. Further, the Company recorded a non-cash loss of $3,845,800 due to the depressed price of the Enterra units at the time that the Acquisitions Class D shares were exchanged for units of Enterra along with management's decision to sell the Enterra units during the third quarter of 2006. During the year ended December 31, 2005, the Company recorded a non-cash gain from the valuation of the imbedded derivative of $630,900.

The Company recorded a net gain of $10,815,600 on the sale of its equity ownership in Pinnacle during the year ended December 31, 2006 The Company received $13.8 million in cash as a result of the sale. From that amount, the Company deducted $2.0 million due to Enterra and its cost basis in Pinnacle of $957,700 for the net gain of $10,815,600. No similar gain was recorded during 2005.

Operating costs and expenses incurred in operations during the year ended December 31, 2005 increased $1,117,700 over those costs and expenses recognized from operations during the prior year. Expenses from real estate operations remained constant during the year ended December 31, 2005 when compared with those expenses incurred during the year ended December 31, 2004. Mineral holding costs increased during the year ended December 31, 2005 over those cost recorded during the previous year by $256,300. The increase in mine holding costs were as a result of increased activity on the properties that the Company holds for the development of uranium and gold as well as work done on the molybdenum property returned by PD.

General and administrative costs and expenses increased by $2,985,500 during the year ended December 31, 2005 when compared with the general and administrative costs and expenses recognized during the year ended December 31, 2004. The primary reasons for these increases were: increased labor costs associated with additional professional staff to evaluate the Company and Crested's mineral properties and a bonus associated with the sale of RMG; increased professional services associated with the Nukem arbitration hearing as well the litigation with PD; costs associated with the adoption of Sarbanes Oxley; and work performed on the SGMI property evaluations and associated increased general and administrative expenses of SGMI.

One outside director of RMG was paid a bonus of $10,000 and another RMG director was paid a bonus of $5,000 for their work on the development of RMG, and the four outside directors of USE were paid $5,000 each for a total bonus to the directors of $35,000. The employees were paid a total bonus of $435,800 at the close of the sale of RMG. All employees of the Company participated in the bonus which was paid at the close of the sale of RMG. The bonus was paid in consideration for the dedicated work put forth by the employees in the development of RMG and due to the fact that many of the employees have not received increases in compensation for a number of years.

Officers of the Company, USE and RMG received the following bonuses: Mark Larsen, President of RMG $140,000, officers of the Company and USE – Keith Larsen and Scott Lorimer $40,000 each, and John L. Larsen, Daniel P. Svilar and Harold F. Herron $20,000 each. In addition to these officers, Mr. Steve Youngbauer who serves as Assistant General Counsel to Mr. Svilar, received a bonus of $40,000. There were two additional members of John L. Larsen's family who received bonuses for a total compensation amount of bonuses to Mr. Larsen's family of $226,000. The total amount paid in bonuses to the directors, officers and employees for work in closing the Enterra purchase of RMG was $470,800 which represents 2.5% of the total consideration received by the Company and its affiliates from the sale of RMG to Enterra.

As a result of increased market prices for uranium the reclamation of these properties was moved further out into the future which resulted in $2,075,900 being reversed out of asset retirement obligation expense. This reversal of cost was offset against the amount of reclamation liability accreted during the year ended December 31, 2005 which resulted in a net cost and expense reduction of $1,709,200.

During the year ended December 31, 2005, other income and expenses resulted in a loss of $484,000 while other income and expenses recognized during the year ended December 31, 2004 resulted in income of $465,100. The primary changes in other income during the year ended December 31, 2005 were (1) a gain of $1,311,200 recognized on the sale of assets, (2) a gain of $1,038,500 from the sale of marketable securities, (3) a decrease of $538,600 in the revenues recorded from the sale of investments (4) gain on the valuation of the derivative associated with the Acquisitions Class D shares of $630,900 discussed above (5) dividend income of $44,700 (6) an increase of $69,400 in interest income over interest income recognized during the previous year. These increases in other income were offset by a significant increase in interest expense of $3,458,900 over the interest expense recognized during the previous year to a total of $4,032,200 in interest expense during the year ended December 31, 2005.

Report of Independent Registered Public Accounting Firm

U.S. Energy Corp. Board of Directors

We have audited the accompanying consolidated balance sheet of U.S. Energy Corp. and subsidiaries as of December 31, 2005 and the related consolidated statements of operations, shareholders' equity and cash flows for each of the two years in the period ended December 31, 2005. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion of these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of U.S. Energy Corp. and subsidiaries as of December 31, 2005 and the results of their operations and their cash flows for each of the two years in the period ended December 31, 2005, in conformity with accounting principles generally accepted in the United States of America.

/s/ EPSTEIN WEBER & CONOVER, PLC

Scottsdale, Arizona
March 3, 2006

U.S. ENERGY CORP. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
LIABILITIES AND SHAREHOLDERS' EQUITY

	December 31, 2006	December 31, 2005
CURRENT LIABILITIES:		
Accounts payable	$ 1,115,000	$ 433,000
Accrued compensation expense	1,190,200	177,100
Current portion of asset retirement obligations	--	233,200
Current portion of long-term debt	937,200	156,500
Refundable deposits	800,000	--
Liabilities held for sale	7,375,800	--
Other current liabilities	177,000	232,400
Total current liabilities	11,595,200	1,232,200
LONG-TERM DEBT, net of current portion	294,900	880,300
ASSET RETIREMENT OBLIGATIONS, net of current portion	124,400	5,669,000
OTHER ACCRUED LIABILITIES	462,700	1,400,500
MINORITY INTERESTS	4,700,200	1,767,500
COMMITMENTS AND CONTINGENCIES		
FORFEITABLE COMMON STOCK, $.01 par value 297,540 and 442,740 shares issued, respectively forfeitable until earned	1,746,600	2,599,000
PREFERRED STOCK, $.01 par value; 100,000 shares authorized No shares issued or outstanding	--	--
SHAREHOLDERS' EQUITY:		
Common stock, $.01 par value; unlimited shares authorized; 19,659,591 and 18,825,134 shares issued net of treasury stock, respectively	196,600	188,200
Additional paid-in capital	72,990,700	68,005,600
Accumulated deficit	(39,101,900)	(40,154,100)
Treasury stock at cost, 497,845 and 999,174 shares respectively	(923,500)	(2,892,900)
Unrealized gain (loss) on marketable securities	306,000	(98,100)
Unallocated ESOP contribution	(490,500)	(490,500)
Total shareholders' equity	32,977,400	24,558,200
Total liabilities and shareholders' equity	$ 51,901,400	$ 38,106,700

The accompanying notes are an integral part of these statements.

U.S. ENERGY CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS

	Year ended December 31,		
	2006	2005	2004
OPERATING REVENUES:			
Real estate operations	$ 217,700	$ 286,000	$ 256,100
Management fees and other	595,700	563,500	559,500
	813,400	849,500	815,600
OPERATING COSTS AND EXPENSES:			
Real estate operations	309,700	306,300	295,500
Mineral holding costs	2,312,800	1,376,300	1,120,000
Asset retirement obligations	854,600	(1,709,200)	346,700
General and administrative	14,007,000	6,943,000	3,957,500
Provision for doubtful accounts	--	--	79,000
	17,484,100	6,916,400	5,798,700
LOSS BEFORE INVESTMENT AND PROPERTY TRANSACTIONS:	(16,670,700)	(6,066,900)	(4,983,100)
OTHER INCOME & (EXPENSES):			
Gain on sales of assets	3,063,600	1,311,200	46,300
(Loss) gain on sale of marketable securities	(867,300)	1,038,500	--
Gain on sale of investments	10,815,600	117,700	656,300
(Loss) gain from valuation of derivatives	(630,900)	630,900	--
Loss from Enterra share exchange	(3,845,800)	--	--
Settlement of litigation	(7,000,000)	--	--
Dividends	147,800	44,700	--
Interest income	732,300	405,200	335,800
Interest expense	(112,600)	(4,032,200)	(573,300)
	2,302,700	(484,000)	465,100
LOSS BEFORE MINORITY INTEREST, DISCONTINUED OPERATIONS AND INCOME TAXES	(14,368,000)	(6,550,900)	(4,518,000)
MINORITY INTEREST IN LOSS OF CONSOLIDATED SUBSIDIARIES	88,600	185,000	207,800
LOSS BEFORE DISCONTINUED OPERATIONS AND INCOME TAXES	(14,279,400)	(6,365,900)	(4,310,200)
DISCONTINUED OPERATIONS, net of taxes			
Gain on sale of discontinued segment	--	15,533,500	--
Loss from discontinued operations	--	(326,100)	(1,938,500)
	--	15,207,400	(1,938,500)
(LOSS) INCOME BEFORE INCOME TAXES	(14,279,400)	8,841,500	(6,248,700)

The accompanying notes are an integral part of these statements.

U.S. ENERGY CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(continued)

	Year ended December 31,		
	2006	2005	2005
NON-CASH INVESTING AND FINANCING ACTIVITIES:			
Conversion of Enterra shares to tradable units	$ 13,880,100	$ --	$ --
Issuance of stock warrants in conjunction with agreements	$ 727,300	$ --	$ --
Acquisition of assets through issuance of debt	$ 355,800	$ 113,400	$ --
Unrealized loss/gain	$ 557,000	$ --	$ --
Satisfaction of receivable - employee with stock in company	$ 30,600	$ 20,500	$ 20,500
Issuance of stock warrants in conjunction with debt	$ --	$ 2,781,200	$ 291,500
Issuance of stock as conversion of subsidiary stock	$ --	$ 1,165,600	$ --
Issuance of stock for services	$ --	$ 100,000	$ --
Issuance of stock to satisfy debt	$ --	$ 4,000,000	$ 1,072,900
Foreclosure of note receivable Cactus Group	$ --	$ 2,926,400	$ --

The accompanying notes are an integral part of these statements.

Stock Based Compensation

SFAS 123, "Accounting for Stock-Based Compensation," ("SFAS 123") defines a fair value based method of accounting for employee stock options or similar equity instruments. SFAS 123 allowed the continued measurement of compensation cost for such plans using the intrinsic value based method prescribed by APB Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB 25"), provided that pro forma disclosures are made to net income or loss and net income or loss per share, assuming the fair value based method of SFAS 123 had been applied. The Company has elected to account for its stock-based compensation plans under APB25 through 2005. Effective January 1, 2006, the Company adopted Statement of Financial Accounting Standards No. 123 (revised 2004), Share-Based Payment ("SFAS 123R"), which requires the Company to measure the cost of employee services received in exchange for all equity awards granted including stock options based on the fair market value of the award as of the grant date. SFAS 123R supersedes Statement of Financial Accounting Standards No. 123, Accounting for Stock-Based Compensation ("SFAS 123") and Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees ("APB 25"). The Company has adopted SFAS 123R using the modified prospective method. Accordingly, prior period amounts have not been restated. Under the modified prospective method, stock options awards that are granted, modified or settled after December 31, 2005 will be valued at fair value in accordance with provisions of SFAS 123R and recognized on a straight line basis over the service period of the entire award.

The effect of implementing SFAS No. 123(R) was an increase in compensation cost recognized in the year ended December 31, 2006 of $273,600.

The Company has computed the fair values of its options granted using the Black-Scholes pricing model and the following weighted average assumptions:

	Year Ended December 31,		
	2006	2005	2004
Risk-free interest rate	4.53%	4.38%	4.82%
Expected lives (years)	4.80	6.75	7.10
Expected volatility	71.02%	78.10%	50.79%
Expected dividend yield	--	--	--

To estimate expected lives of options for this valuation, it was assumed options will be exercised at the end of their expected lives. All options are initially assumed to vest. 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.

If the Company had accounted for its stock-based compensation plans in accordance with SFAS 123 during the years ended December 31, 2005 and 2004, the Company's net gain/(loss) and pro forma net gain/(loss) per common share would have been reported as follows:

	Year Ended December 31,	
	2005	2004
Net gain (loss) to common shareholder as reported	$ 8,841,500	$ (6,248,700)
Deduct: Total stock based employee expense determined under fair value based method		
U.S. Energy employee options	(3,617,900) [1]	(207,100)
Subsidiary employee options	(1,013,500) [2]	--
Pro forma net loss	$ 4,210,100	$ (6,455,800)

	2005	2004
As reported, Basic	$ 0.55	$ (0.47)
As reported, Diluted	$ 0.55	$ (0.47)
Pro forma, Basic	$ 0.26	$ (0.49)
Pro forma, Diluted	$ 0.25	$ (0.49)

(1) Includes the accelerated vesting of 804,000 employee options which were exercisable at $2.46 per share and would have vested at the rate of 268,000 shares each on July 1, 2007, 2008 and 2009. Employees who hold the options have a 21.7 year weighted average employment history with the Company and do not plan to retire. The options would not have been forfeited had they not been accelerated.

(2) On September 2, 2004, the Board of Directors of Crested adopted (and the shareholders approved) the 2004 Incentive Stock Option Plan (the "2004 ISOP") for the benefit of Crested's key employees. The 2004 ISOP reserves for issuance shares of the Company's common stock equal to 20% of the Company's shares of common stock issued and outstanding at any time and has a term of 10 years. During the year ended December 31, 2005, Crested issued 1,700,000 options under this plan to employees of USE. These options were valued for purposes of this footnote using a 4.38% Risk-free interest rate, expected lives of 9.4 years and an expected volatility of 107%.

Weighted average shares used to calculate pro forma net loss per share were determined as described in Note B, except in applying the treasury stock method to outstanding options, net proceeds assumed received upon exercise were increased by the amount of compensation cost attributable to future service periods and not yet recognized as pro forma expense.

Income Taxes

The Company accounts for income taxes under the provisions of Statement of Financial Accounting Standards No. 109 ("SFAS 109"), "Accounting for Income Taxes". This statement requires recognition of deferred income tax assets and liabilities for the expected future income tax consequences, based on enacted tax laws, of temporary differences between the financial reporting and tax bases of assets, liabilities and carry forwards.

SFAS 109 requires recognition of deferred tax assets for the expected future effects of all deductible temporary differences, loss carry forwards and tax credit carry forwards. Deferred tax assets are reduced, if deemed necessary, by a valuation allowance for any tax benefits which, based on current circumstances, are not expected to be realized.

Net Gain (Loss) Per Share

The Company reports net gain (loss) per share pursuant to Statement of Financial Accounting Standards No. 128 ("SFAS 128"). SFAS 128 specifies the computation, presentation and disclosure requirements for earnings per share. Basic earnings per share are computed based on the weighted average number of common shares outstanding. Common shares held by the ESOP are included in the computation of earnings per share. Total shares held by the ESOP at December 31, 2006 were 525,881 shares which are allocated to participant accounts and 155,811 shares held as collateral for loans to the Company. 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 to purchase common stock, if dilutive. Using the treasury stock method there were 2,372,361 potential shares relating to forfeitable shares, options and warrants that are included in the diluted earnings per share for 2006. Potential common shares relating to options and warrants are excluded from the computation of diluted loss per share, because they were antidilutive, totaled 5,928,102 and 5,628,820 at December 31, 2005, and 2004, respectively.

Diluted Earnings Per Share

	2006		
	Income	Shares	Per Share
Basic earning per share	$ 1,052,200	18,461,885	$ 0.06
Effect of dilutive securities:			
Forfeitable shares		297,540	
Outstanding options		1,780,005	
Outstanding warrants		592,356	
		2,669,901	
Diluted earning per share:	$ 1,052,200	21,131,786	$ 0.05

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles in the USA requires management to make estimates and 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. Actual results could differ from those estimates.

Reclassifications

Certain reclassifications have been made in the prior years financial statements in order to conform to the presentation for the current year.

Recent Accounting Pronouncements

FIN 48 In June 2006, the FASB issued FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes," ("FIN 48") an interpretation of FASB Statement No. 109, "Accounting for Income Taxes." FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 requires that the Company recognize in its financial statements, the impact of a tax position, if that position is more likely than not of being sustained on audit, based on the technical merits of the position. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods and disclosure. The provisions of FIN 48 are effective beginning January 1, 2007 with the cumulative effect of the change in accounting principle recorded as an adjustment to the opening balance of retained earnings, goodwill, deferred income taxes and income taxes payable in the Consolidated Balance Sheets. The Company does not expect that the adoption of FIN 48 will have a significant impact on the financial statements of the Company.

FAS 157 In September 2006, the FASB issued FASB Statement No. 157, "Fair Value Measurements" ("FAS 157"). FAS 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. The provisions for FAS 157 are effective for the Company's fiscal year beginning January 1, 2008. The Company is currently evaluating the impact that the adoption of this statement will have on the Company's consolidated financial position, results of operations or cash flows.

In September 2006, the Securities and Exchange Commission issued Staff Accounting Bulletin No. 108, *Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements* ("SAB 108"). SAB 108 provides guidance on consideration of the effects of prior year misstatements in quantifying current year misstatements for the purpose of a materiality assessment. SAB 108 is effective for fiscal years ending after November 15, 2006. The adoption of SAB 108 did not have an impact on our consolidated financial statements.

Rocky Mountain Gas, Inc.

In 1999, the Company and Crested organized Rocky Mountain Gas, Inc. ("RMG") to enter into the coalbed methane gas/natural gas business. RMG was engaged in the acquisition of coalbed methane gas properties and the future exploration, development and production of methane gas from those properties.

On June 1, 2005, Enterra US Acquisitions Inc. ("Acquisitions") (a privately-held Washington corporation organized by Enterra Energy Trust ("Enterra") acquired all the outstanding stock of RMG, for which Enterra paid $500,000 cash and issued $5,234,000 of Enterra units (the "Enterra Initial Units"), net of the $266,000 adjustment for the purchase of overriding royalty interests (effected May 1, 2005); and Acquisitions issued $14,000,000 of Class D shares of Acquisitions. The Enterra Initial Units and the Class D shares were issued pro rata to the RMG shareholders. USE's and Crested's participation in the consideration received was approximately $18,341,600. USE's consolidated subsidiary, Yellowstone Fuels, Inc. ("YSFI") also received approximately $296,700.

The Enterra Initial Units received by the Company and Crested were sold during the quarter ended September 30, 2005 resulting in a gain of $1,038,500. The carrying value of the Initial Units received by YSFC are reflected on the Company's consolidated balance sheet at December 31, 2005 was $77,100 in marketable securities and the Class D shares of Acquisitions received by the Company, Crested and YSFI are carried as $13,803,200 as investments in non-affiliates. The Company and its subsidiaries converted the Enterra Acquisitions Class D shares into shares of Enterra Energy Trust which were then saleable on the Toronto Stock Exchange – Vancouver ("TSX-V") on a one for one basis during 2006. The Company and Crested sold 682,345 units during the period ended December 31, 2006 for which they received $8,304,300 in cash proceeds. At December 31, 2006 the Company retained an investment of $123,400 on a consolidated basis as a result of YSFI not selling any of the shares it received.

For further discussion of the sale of RMG please see Note L, Discontinued Operations.

Pinnacle

On June 23, 2003, a Subscription and Contribution Agreement was executed by RMG, CCBM, a wholly owned subsidiary of Carrizo Oil and Gas, Inc. and seven affiliates of Credit Suisse First Boston Private Equity ("CSFB Parties"). Under the Agreement, RMG and CCBM contributed certain of their respective interests, having an estimated fair value of approximately $7.5 million each, carried on RMG's books at a cost of $957,600, comprised of (1) leases in the Clearmont, Kirby, Arvada and Bobcat CBM project areas and (2) oil and gas reserves in the Bobcat project area, to a newly formed entity, Pinnacle Gas Resources, Inc., a Delaware corporation ("Pinnacle"). In exchange for the contribution of these assets, RMG and CCBM each received 37.5% of the common stock of Pinnacle ("Pinnacle Common Stock") as of the closing date and options to purchase Pinnacle Common Stock ("Pinnacle Stock Options"). CFSB contributed $5.0 million for 25% of the common stock of Pinnacle and agreed under certain terms to fund additional acquisition and development programs.

The Pinnacle shares (which had been owned by RMG, but were not sold as part of the 2005 Enterra transaction) were transferred to the Company and Crested in 2005. The transaction with Enterra required the Company and Crested to pay Enterra if the Pinnacle shares were later sold for more than $10 million; the payment (allowed to be by either cash or the Company's common stock) would be the difference between $10 million and proceeds of sale (but not more than $2 million). In September 2006, the Company and Crested sold their Pinnacle shares in a private transaction for $13.8 million cash, and recorded a gain on the transaction of $10,815,600. As a result of the sale of the Pinnacle shares, the Company and Crested became obligated to pay Enterra $2.0 million in either cash or common stock of the Company. In 2006, the Company and Crested paid the obligation to Enterra with 506,395 shares (valued at $3.95 per share at the time) of the Company's common stock (with a market value of $2 million) owned by Crested. Crested recorded a payment of $700,000 (35% of the $2.0 million, representing its share of RMG before it was sold), and a credit on its debt to the Company in the amount of $1.3 million.

Crested also returned 6,030 additional shares it owned to the Company for which it received an additional credit of $23,800 against its debt to the Company.

G. DEBT

As of December 31, 2006 and 2005 the Company and its subsidiaries had current and long term liabilities associated with deferred rents, leases, self funding of employee health insurance, accrued holding costs of uranium properties and accrued retirement costs.

Other current liabilities:

	December 31,	
	2006	2005
Employee health insurance self funding	$ 60,000	$ 101,200
Deferred rent	28,200	25,500
Accrued expenses	21,800	36,100
Mineral property lease	67,000	69,700
	$ 177,000	$ 232,500

Other long term liabilities:

	2006	2005
Accrued retirement costs	$ 462,700	$ 43,300
Holding costs of uranium property	--	1,357,200
	$ 462,700	$ 1,400,500

The Company has a $500,000 line of credit from a commercial bank. The line of credit has a variable interest rate (9.25% as of December 31, 2006). The weighted average interest rate for the year ended December 31, 2006 was 8.96%. As of December 31, 2006, none of the line of credit had been borrowed. The line of credit is collateralized by certain real property.

The income tax provision is different 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:

	December 31,		
	2006	2005	2004
Expected federal income tax expense (benefit)	$ (4,997,800)	$ (1,967,100)	$ (2,133,800)
Dividends received deduction	--	(1,700,000)	--
Net operating loss utilized	--	--	(1,429,700)
Interest expense adjustment	--	1,190,400	--
Prior year true-up & rate change	(1,214,600)	--	--
Permanent differences	1,225,100	--	--
Inclusion of Crested's prior year NOL and AMT credit	(4,323,700)	--	--
Increase (decrease) in valuation allowance	(6,020,600)	2,476,700	3,563,500
Deferred income tax benefit	$ (15,331,600)	$ --	$ --

There were no taxes payable at December 31, 2006 and 2005.

Crested's NOL and AMT credits were erroneously excluded from the 2005 and 2004 disclosure. The result of that exclusion had no effect on the net deferred income tax assets or liabilities in those years.

At December 31, 2006, the Company (together with Crested Corp.) had available, for federal income tax purposes, net operating loss carry forwards ("NOL") of approximately $41,500,300 which will expire from 2008 to 2026.

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

I. SEGMENTS AND MAJOR CUSTOMERS:

During the years ended December 31, 2004 and 2003 the Company had business activities in coalbed methane gas property acquisition, exploration and production. The Company also had a reportable industry segment in commercial activities through motel, real estate and airport operations. The Company sold RMG on June 1, 2005 which resulted in only one business segment, commercial activities which during the year ended December 31, 2006 were all being managed by third parties and the Company only recognized management fee revenues. No presentation of business segments is therefore made at December 31, 2006 as all coalbed methane gas operations are accounted for as discontinued operations.

During the years ended December 31, 2006, 2005 and 2004 the following activity occurred under the 1998 ISOP:

	Year ended December 31,		
	2006	2005	2004
Grants			
Qualified	--	--	--
Non-Qualified	--	--	--
	--	--	--
Price of Grants			
High	--	--	--
Low	--	--	--
Exercised			
Qualified	83,529	142,907	--
Non-Qualified	20,109	55,234	--
	103,638	198,141	--
Total Cash Received	$ - [1]	$ 132,600 [2]	$ -
Forfeitures/Cancellations			
Qualified	--	--	--
Non-Qualified	--	--	--
	--	--	--

[1] All options were exercised by the exchange of 46,863 shares valued at $254,600.

[2] In addition to the cash exercise of options shares valued at $389,600 were exchanged for the exercise of 142,907 of the total shares exercised.

In December 2001, 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 USE's key employees. The 2001 ISOP (amended in 2004 and approved by the shareholders) reserves for issuance shares of the Company's common stock equal to 20% of the Company's shares of common stock issued and outstanding at any time. The 2001 ISOP has a term of 10 years.

During the years ended December 31, 2006, 2005 and 2004 the following activity occurred under the 2001 ISOP:

	Year ended December 31,		
	2006	2005	2004
Grants			
Qualified	25,000	13,160	1,272,000
Non-Qualified	--	686,840	--
	25,000	700,000	1,272,000
Price of Grants			
High	$ 4.09	$ 3.86	$ 2.46
Low	$ 4.09	$ 3.86	$ 2.46
Exercised			
Qualified	169,393	225,426	--
Non-Qualified	79,865	79,303	--
	249,258	304,729	--
Total Cash Received	$ 198,100 [1]	$ 173,700 [2]	$ --
Forfeitures/Cancellations			
Qualified		65,000	12,000
Non-Qualified		--	--
	--	65,000	12,000

[1] In addition to the cash exercise of options there were 132,874 shares valued at $687,200 exchanged for exercises of 177,952 options.

[2] In addition to the cash exercise of options shares valued at $557,300 were exchanged for the exercise of 240,404 of the total shares exercised.

The 2001 ISOP replaces the 1998 ISOP, however, options granted under the 1998 ISOP remain exercisable until their expiration date under the terms of that Plan.

The following table represents the activity in employee options for the periods covered by the Annual Report for the year ended December 31, 2006 that are not in employee stock option plans:

	Year ended December 31,		
	2006	2005	2004
Grants			
Qualified	--	--	--
Non-Qualified	--	--	--
	--	--	--
Price of Grants			
High	--	--	--
Low	--	--	--
Exercised			
Qualified	--	--	--
Non-Qualified	--	--	--
	--	--	--
Total Cash Received	--	--	--
Forfeitures/Cancellations			
Qualified	--	--	--
Non-Qualified	--	--	10,000
	--	--	10,000

A summary of the Employee Stock Option Plans activity in all plans for the year ended December 31, 2006, 2005 and 2004 is as follows:

	Year ended December 31,					
	2006		2005		2004	
	Options	Weighted Average Exercise Price	Options	Weighted Average Exercise Price	Options	Weighted Average Exercise Price
Outstanding at beginning of the period	4,255,776	$ 2.88	4,123,646	$ 2.66	2,873,646	$ 2.74
Granted	25,000	$ 4.09	700,000	$ 3.86	1,272,000	$ 2.46
Forfeited			(65,000)	$ 2.46	(22,000)	$ 2.66
Expired				--	--	--
Exercised	(352,896)	$ 2.51	(502,870)	$ 2.50	--	--
Outstanding at period end	3,927,880	$ 2.92	4,255,776	$ 2.88	4,123,646	$ 2.66
Exercisable at period end	3,902,880	$ 2.91	4,017,776	$ 2.90	2,863,646	$ 2.74
Weighted average fair value of options granted during the period		$ 3.38		$ 3.64		$ 1.66

The exercise of 352,896 options resulted in the net issuance of 220,022 shares. The options were exercised due to the payment of cash for 71,307 shares and cashless exercise of 281,589 options as a result of the cancellation of 132,874 shares.

No expense was recognized as a result of the issuance of 25,000 options during 2006 as the options vest over five years and the grant of the options was late in the fourth quarter of 2006 so any compensation expense is immaterial. Over the life of these options, seven years, the Company will recognize $84,500 in compensation expense. The option expense will be recognized over the five year vest period based on the Black Scholes model which utilizes anticipated forfeiture of Company options as well as volatility in the market price of the Company's common stock.

The following table summarized information about employee stock options outstanding and exercisable at December 31, 2006:

Grant Price Range	Options Outstanding at December 31, 2006	Weighted average remaining contractual life in years		Weighted average exercise price		Options exercisable at December 31, 2006	Weighted average exercise price	
$2.00	230,981	$	1.74	$	2.00	230,981	$	2.00
$2.01 - $2.25	415,266	$	4.93	$	2.25	415,266	$	2.25
$2.26 - $2.40	784,540	$	4.02	$	2.40	784,540	$	2.40
$2.41 - $2.46	963,051	$	7.50	$	2.46	963,051	$	2.46
$2.47 - $2.88	147,346	$	1.74	$	2.88	147,346	$	2.88
$2.89 - $3.86	683,768	$	8.78	$	3.86	683,768	$	3.86
$3.87 - $3.90	677,928	$	4.93	$	3.90	677,928	$	3.90
$3.91 - $4.09	25,000	$	9.75	$	4.09	-	$	-
	3,927,880	$	5.77	$	2.92	3,902,880	$	2.91

The following table sets forth the number of options available for grant as well as the intrinsic value of the options outstanding and exercisable:

		2006		2005		2004
Available for future grant		1,166,905		775,756		387,247
Intrinsic value of option exercised	$	885,500	$	1,255,200	$	-
Aggregate intrinsic value of options outstanding	$	8,378,300	$	6,399,800	$	1,916,900
Aggregate intrinsic value of options exercisable	$	8,354,300	$	5,942,800	$	1,280,900

Employee Stock Ownership Plan

The Board of Directors of the Company adopted the U.S. Energy Corp. 1989 Employee Stock Ownership Plan ("ESOP") in 1989, for the benefit of all the Company's employees. Employees become eligible to participate in the ESOP after one year of service which must consist of at least 1,000 hours worked. After the employee becomes a participant in the plan he or she must have a minimum of 1,000 hours of service in each plan year to be considered for allocations of funding from the Company. Employees become 20% vested after three years of service and increase their vesting by 20% each year thereafter until such time as they are fully vested after eight years of service. An employee's total compensation paid, which is subject to federal income tax, up to an annual limit of $220,000, $210,000 and $201,000 for the years ended December 31, 2006, 2005 and 2004, respectively is the basis for computing how much of the total annual funding is contributed into his or her personal account. An employee's compensation divided by the total compensation paid to all plan participants is the percentage that each participant receives on an annual basis. The Company funds 10% of all eligible compensation annually in the form of common stock and may fund up to an additional 15% to the plan in common stock. As of December 31, 2006, all shares of the Company's stock that have been contributed to the ESOP have been allocated. The estimated fair value of shares that are not vested is approximately $196,100.

During the year ended December 31, 2006 the Board of Directors of the Company approved a contribution of 70,756 shares to the ESOP at the price of $4.98 for a total expense of $352,300. This compares to contributions to the ESOP during the year ended December 31, 2005 and 2004 of 56,494 and 70,439 shares to the ESOP at prices of $4.65 and $2.96 per share, respectively. The Company has expensed $352,300 $262,600 and $208,500 during the years ended December 31, 2006, 2005 and 2004 respectively related to these contributions.

During prior years the Company loaned the ESOP $1,014,300 to purchase 125,000 shares from the Company and 38,550 shares on the open market. The Company paid the ESOP 2,350 shares as dividends on the shares the ESOP had purchased. During the year ended May 31, 1996, 10,089 of these shares were used to fund the Company's annual funding commitment and reduce the loan to the Company by $87,300. During a previous year the loans were also adjusted by $436,500 to reflect their value at the time. The loans at December 31, 2006 are reflected as unallocated ESOP contribution of $490,500 in the equity section of the accompanying Consolidated Balance Sheets and are secured by 155,811 unallocated shares purchased under the loan.

Warrants to Others

As of December 31, 2006, there were 1,821,323 warrants outstanding to purchase shares of the Company's common stock. The Company values these warrants using the Black-Scholes option pricing model and expenses that value over various terms based on the nature of the award. Activity for the periods ended December 31, 2006 for warrants is represented in the following table:

	Year ended December 31,					
	2006		2005		2004	
	Warrants	Weighted Average Exercise Price	Warrants	Weighted Average Exercise Price	Warrants	Weighted Average Exercise Price
Outstanding at beginning of the period	1,672,326	3.44	1,505,174	$ 3.35	907,209	$ 3.51
Granted	425,012	4.39	1,396,195	$ 3.70	868,465	2.87
Forfeited	-		(316,968)	$ 3.41	(145,500)	2.63
Expired	(50,000)	3.63	(1,713)	$ 3.00	--	--
Exercised	(226,015)	3.84	(910,362)	$ 3.65	(125,000)	2.01
Outstanding at period end	1,821,323	3.61	1,672,326	$ 3.47	1,505,174	$ 3.35
Exercisable at period end	1,821,323	3.61	1,642,326	$ 3.49	1,044,152	$ 3.43
Weighted average fair value of options granted during the period		$ 1.69		$ 1.37		$ 0.79

During the year ended December 31, 2006 the Company issued a total of 425,012 new warrants to investors and financing entities. 100,000 warrants exercisable at $7.15 per share with an expiration date of June 5, 2009, for which a non cash expense of $251,800 was recognized, were issued to Cornell Capital as a result of the issuance by Cornell Capital of a $50 million equity line of credit which was subsequently cancelled. The Company also issued 225,000 warrants to prior investors to settle various disputes which are exercisable at $3.25 per share and expire on August 25, 2009. 16,103 warrants were issued as a result of anti dilution provisions in original warrants issued to four previous investors. These warrants have exercise prices ranging from $2.87 per share to $3.56 per share and expire beginning in January 2008 through April 2010. 25,000 warrants included as new issuance warrants are previously existing warrants which were re-assigned to a third party by the original investor. These warrants have a strike price of $5.48 and expire in February 2008. An additional 58,909 warrants were extended due to the lapse of registration coverage. These warrants range in exercise price from $3.00 to $4.00 per share and expire on October 31, 2007. A non cash expense of $484,700 was recognized as a result of the extension of these warrants.

The following table summarized information about non employee warrants outstanding and exercisable at December 31, 2006:

Grant Price Range	Warrants Outstanding at December 31, 2006	Weighted average remaining contractual life in years	Weighted average exercise price	Warrants exercisable at December 31, 2006	Weighted average exercise price
$2.00 - $2.40	50,000	3.75	$ 2.26	50,000	$ 2.26
$2.46 - $2.88	415,418	4.40	$ 2.72	415,418	$ 2.72
$3.00 - $3,25	321,747	2.19	$ 3.22	321,747	$ 3.22
$3.56 - $3.75	443,452	1.06	$ 3.64	443,452	$ 3.64
$3.81 - $3.90	265,000	5.62	$ 3.86	265,000	$ 3.86
$4.00 - $4.30	225,706	1.19	$ 4.16	225,706	$ 4.16
$7.15	100,000	2.43	$ 7.15	100,000	$ 7.15
	1,821,323	2.85	$ 3.61	1,821,323	$ 3.61

These warrants are held by persons or entities other than employees, officers and directors of the Company.

Forfeitable Shares

Certain of the shares issued to officers, directors, employees and third parties are forfeitable if certain conditions are not met. Therefore, these shares have been reflected outside of the Shareholders' Equity section in the accompanying Consolidated Balance Sheets until earned. During fiscal 1993, the Company's Board of Directors amended the stock bonus plan. As a result, the earn-out dates of certain individuals were extended until retirement. The Company recorded $126,100 of compensation expense for the year ended December 31, 2006 compared to $171,100 and $216,800 for the years ended December 31, 2005 and 2004 respectively. The accompanying balance sheet at December 31, 2006 includes a deferred charge of $25,400 which is included in prepaid expenses. A schedule of total forfeitable shares for the Company is set forth in the following table:

Issue Date	Number of Shares	Issue Price	Total Compensation
Balance at December 31, 2004 and December 31, 2005	442,740		$ 2,599,000
Shares earned	(145,200)	--	(852,400)
Balance at December 31, 2006	297,540		$ 1,746,600

K. COMMITMENTS, CONTINGENCIES AND OTHER:

LEGAL PROCEEDINGS

Material legal proceedings pending at December 31, 2006, and developments in those proceedings from that date to the date this Annual Report is filed, are summarized below. Legal proceedings which were not material to the Company were concluded in the fourth quarter 2006.

Phelps Dodge – Lucky Jack Molybdenum Property

On September 26, 2006, the Company signed a Settlement Agreement and Release with Phelps Dodge Corporation ("PD") resulting in a $7,000,000 payment to PD as part of the final agreement. This settlement resulted in a cash savings of $538,300 from the $7,538,300 awarded to PD by the U.S. Federal District Court of Colorado on July 26, 2006.

Patent Claims Litigation – Lucky Jack Molybdenum Property

The only pending legal proceeding to which the Company and Crested are parties relates to a challenge to the validity of title to the patented claims included in the molybdenum property.

On April 2, 2004, the United States Bureau of Land Management ("BLM") issued patents on nine additional mining claims for the Lucky Jack molybdenum property (previously known as Mount Emmons), for a total of 25 patented claims which consists of approximately 350 patented or "fee" acres. A lawsuit was filed by local governmental entities and environmentalists ("Appellants") in U.S. District Court of Colorado challenging BLM's issuance of the nine additional mining patents and alleging BLM violated the 1872 Mining Law, applicable regulations, and the Administrative Procedures Act by overruling their protests to Mt. Emmons Mining Company's mineral patent application, by awarding the patents, and by conveying the land to Mt. Emmons Mining Company (a subsidiary of Phelps Dodge Corporation). The case was High Country Citizen's Alliance, Town of Crested Butte, Colorado, and The Board of County Commissioners of the County of Gunnison, Colorado v. Kathleen Clarke, Director of the Bureau of Land Management et. al., Gale Norton, Secretary of Interior, U.S. Department of the Interior; Phelps Dodge Corporation; Mt. Emmons Mining Company.

On January 12, 2005, U.S. District Court dismissed the Appellants' appeal holding: (i) that they had no right of appeal from a decision to issue a mineral patent, because the 1872 Mining Law created no private cause of action for unrelated parties to challenge the issuance of a mineral patent, and (ii) because the 1872 Mining Law implicitly precludes unrelated third parties from challenging mineral patent by judicial action, the Administrative Procedures Act does not constitute a waiver of sovereign immunity for purposes of the action. Appellants filed an appeal of the U.S. District Court's decision to the United States Tenth Circuit Court of Appeals (10th CAA"). The 10th CCA case number is D.C. No. 04-MK-749PAC and No. 05-1085.

On February 28, 2006, the property was transferred to the Company and Crested by PD and Mt. Emmons Mining Company. On July 21, 2006, the 10th CAA affirmed the January 12, 2005 dismissal by the U.S. District Court of challenges to the issuance of nine additional mining patents on the molybdenum property. On September 5, 2006, the Appellants filed a Petition for Rehearing En Banc of the July 21, 2006, decision before the entire 10th CCA. On September 8, 2006, the Company and Crested were admitted as substitute parties for Phelps Dodge Corporation and Mt. Emmons Mining Company (following the Company's and Crested's filing of a Motion to Substitute Parties.

On October 27, 2006, the entire 10th CCA affirmed and upheld the July 21, 2006, decision by the 10th CCA panel, thereby denying the Appellants' Petition of Rehearing En Banc and their challenges to the issuance of the patents.

On February 26, 2007, the Appellants filed a petition for certiorari with the United States Supreme Court again arguing that they were improperly denied judicial review of the decision by BLM to issue the patents. The BLM and the Company and Crested must file any opposition briefs on or before March 28, 2007. Management is not able to predict the outcome or the ultimate effect, if any, this litigation will have on the Company.

ASSET RETIREMENT OBLIGATIONS

Sheep Mountain Uranium Properties

The Company is responsible for the reclamation obligations, environmental liabilities and liabilities for injuries to employees in mining operations with respect to the Sheep Mountain uranium properties. The reclamation obligations, which are established by regulatory authorities, were reviewed by the Company and the regulatory authorities and they jointly determined that the reclamation liability at December 31, 2006 was $2.5 million. The Company is self bonded for this obligation by mortgaging certain of their real estate assets, including the Glen L. Larsen building, and by posting cash bonds.

Plateau Resources Limited

The environmental and reclamation obligations acquired with the acquisition of Plateau include obligations relating to the Shootaring Mill. As of December 31, 2006, the present value at 8% of the reclamation liability on the Plateau properties was $4.1 million. Plateau holds a cash deposit for reclamation in the amount of approximately $6.9 million.

If the sale of the uranium properties to Uranium One closes, (see Note B), the asset retirement obligation on the Sheep Mountain and Plateau Resources properties will be transferred to Uranium One. (See Note B, Liabilities Held for Sale).

Sutter Gold Mining Inc.

SGMI's mineral properties are currently on shut down status and have never been in production. There has been minimal surface disturbance on the Sutter properties. Reclamation obligations consist of closing the mine entry and removal of a mine shop. The reclamation obligation to close the property has been set by the State of California at $22,400 which is covered by a cash reclamation bond. This amount was recorded by SGMI as a reclamation liability as of December 31, 2006.

401(K) PLAN

The Board of Directors of USE adopted the U.S. Energy Corp. 401(K) Plan ("401(K)") in 2004, for the benefit of USE employees. The Company matches 50% of an employee's salary deferrals up to a maximum Company contribution per employee of $4,000 annually. The Company expensed $62,300 and $52,800 for the years ended December 31, 2006 and 2005, respectively related to these contributions.

EXECUTIVE OFFICER COMPENSATION

In December 2001, the Board of Directors adopted (and the shareholders approved) the 2001 Stock Award Plan to compensate six of its executive officers. Under the Plan, 10,000 shares may be issued to each officer each year during his employment. During the years ended December 31, 2006, 2005 and 2004 the Company issued 57,500, 60,000 and 50,000 shares of stock to these officers, respectively. The Officers have agreed not to sell the shares granted under the 2001 Stock Award Plan and the Company has agreed to pay all taxes due on the shares granted to the Officers.

The Company and Crested are committed to pay the surviving spouse or dependant children of the former Chairman and Founder, who passed away on September 4, 2006, one years' salary and 50% of that amount annually for an additional four years thereafter. The maximum compensation due under these agreements for the first year is $170,000 and $85,000 thereafter. Certain officers and employees have employment agreements with the Company and Crested.

On October 20, 2005 the Board of Directors of the Company and Crested adopted an Executive Retirement Policy for the Chairman/CEO, Chairman Emeritus, President/COO, CFO/Treasurer/V.P. Finance, Senior Vice President and General Counsel. Under the terms of the Retirement Plan, the retired executive will receive monthly installments in accordance with the normal bi-weekly payroll practices of the Company in the amount of 50% of the greater of (i) that amount of compensation the Executive Officer received as base cash pay on his/her final regular pay check or (ii) the average annual pay rate, less all bonuses, he/she received over the last five years of his/her employment with Company. To be eligible for this benefit, the executive officer must serve in one of the designated executive offices for 15 years, reach the age of 60 and be an employee of USE on December 31, 2010. On September 4, 2006 the founder and former Chairman of the company passed away and General Counsel to the Company announced that he planned to retire in January of 2007. The Board of Directors made a one time exception for these two individuals due to their long and profitable service to the Company and waived the December 31, 2010 requirement. The compensation expense for the year ended December 31, 2006 was $419,400. The total accrued liability at December 31, 2006 for executive retirement was $467,700. The Company has also established a mandatory retirement age of 65 unless the Board specifically requests the services of an employee officer beyond that age.

The employees of the Company are not given raises on a regular basis. In consideration of this and in appreciation of the work they perform bonuses are paid to the employees, officers and directors at the conclusion of major transactions. The recommendation for bonuses are made by the Chairman and ratified, first by the Compensation Committee and second by the full board prior to being paid. Similar bonuses to those paid during prior years may be paid in the future.

OPERATING LEASES

The Company is the lessor of portions of the office buildings and building improvements that it owns. The Company occupies the majority of its main office building. The leases are accounted for as operating leases and expire at various periods through January, 2007, and provide for minimum monthly receipts of $16,400 through December, 2006. All of the Company's leases are for two years or less.

The total costs of the office buildings and building improvements totaled $3,968,400 and $4,213,000 as of December 31, 2006 and 2005 and accumulated depreciation amounted to $2,322,900 and $2,464,900 as of December 31, 2006 and 2005, respectively. Rental income under the agreements was $187,300, $238,200 and $245,000 for the years ended December 31, 2006, 2005 and 2004, respectively.

Future minimum receipts for non-cancelable operating leases are as follows:

Years Ending December 31,	Amount
2007	$92,600
2008	46,000

L. DISCONTINUED OPERATIONS:

On June 1, 2005, the Company and Crested closed on the sale of their interests in RMG to Enterra Energy Trust. The sale agreement states that the effective date of the sale to Enterra was April 1, 2005. Therefore, the revenues and expenditures presented for 2005 as discontinued operations are for the three month period ending March 31, 2005. The financial statements for all of the periods presented have been revised to present these operations as discontinued.

	Year ending December 31,		
	2006	2005	2004
Gain on sale of discontinued segment			
Gain	$ --	$ 15,768,500	$ --
Taxes paid	--	(235,000)	--
	$ --	$ 15,533,500	$ --
Gain (loss) from dicontinued operations			
Rocky Mountain Gas			
Revenues	$ --	$ 1,110,100	$ 3,826,100
Expenditures	--	(1,309,000)	(5,502,300)
Other	--	(127,200)	(262,300)
	$ --	$ (326,100)	$ (1,938,500)
Canyon Homesteads			
Revenues	$ --	$ --	$ --
Expenditures	--	--	--
Other	--	--	--
	$ --	$ --	$ --
Total gain (loss) from dicontinued operations	$ --	$ 15,207,400	$ (1,938,500)

M. SELECTED QUARTERLY FINANCIAL DATA (Unaudited)

U.S. ENERGY CORP.
SELECTED QUARTERLY FINANCIAL DATA (Unaudited)

	Three Months Ended			
	December 31, 2006	September 30, 2006	June 30, 2006	March 31, 2006
Operating revenues	$ 207,400	$ 281,100	$ 148,300	$ 176,600
Operating loss	$ (4,283,900)	$ (6,476,000)	$ (2,967,400)	$ (2,943,400)
Loss from continuing operations	$ (4,024,400)	$ (2,933,700)	$ (6,236,200)	$ (1,085,100)
Discontinued operations, net of tax	$ --	$ --	$ --	$ --
Benefit from income taxes	$ 15,331,600	$ --	$ --	$ --
Net income (loss)	$ 11,307,200	$ (2,933,700)	$ (6,236,200)	$ (1,085,100)
Gain (loss) per share, basic				
Continuing operations	$ 0.60	$ (0.16)	$ (0.34)	$ (0.06)
Discontinued operations	--	--	--	--
	$ 0.60	$ (0.16)	$ (0.34)	$ (0.06)
Basic weighted average shares outstanding	18,991,008	18,367,198	18,300,530	18,127,158
Gain (loss) per share, diluted				
Continuing operations	$ 0.53	$ (0.16)	$ (0.34)	$ (0.06)
Discontinued operations	--	--	--	--
	$ 0.53	$ (0.16)	$ (0.34)	$ (0.06)
Diluted weighted average shares outstanding	21,178,257	18,367,198	18,300,530	18,127,158

U.S. ENERGY CORP.
SELECTED QUARTERLY FINANCIAL DATA (Unaudited)

	Three Months Ended			
	December 31, 2005 (Restated)	September 30, 2005 (Restated)	June 30, 2005 (Restated)	March 31, 2005 (Restated)
Operating revenues	$ 157,500	$ 167,100	$ 183,500	$ 341,400
Operating loss	$ (980,400)	$ (1,481,600)	$ (2,420,900)	$ (1,184,000)
Gain (loss) from continuing operations	$ (4,503,000)	$ 1,228,600	$ (1,819,100)	$ (1,272,400)
Discontinued operations, net of tax	$ --	$ (188,100)	$ 15,721,600	$ (326,100)
Net gain (loss)	$ (4,503,000)	$ 1,040,500	$ 13,902,500	$ (1,598,500)
Gain (loss) per share, basic				
Continuing operations	$ (0.26)	$ 0.06	$ (0.12)	$ (0.09)
Discontinued operations	$ --	$ (0.01)	$ 1.02	$ (0.02)
	$ (0.26)	$ 0.06	$ 0.91	$ (0.11)
Basic weighted average *shares outstanding*	*17,624,085*	*17,229,336*	*15,352,966*	*14,398,093*
Gain (loss) per share, diluted				
Continuing operations	$ (0.25)	$ 0.07	$ (0.12)	$ (0.09)
Discontinued operations	$ --	$ (0.01)	$ 1.00	$ (0.02)
	$ (0.25)	$ 0.06	$ 0.88	$ (0.11)
Diluted weighted average shares outstanding	18,066,825	17,672,076	15,795,706	14,398,093

U.S. ENERGY CORP.
SELECTED QUARTERLY FINANCIAL DATA (Unaudited)

	Three Months Ended			
	December 31, 2004	September 30, 2004	June 30, 2004	March 31, 2004
Operating revenues	$ 264,500	$ 272,300	$ 141,600	$ 137,200
Operating loss	$ (1,124,400)	$ (1,147,500)	$ (1,273,100)	$ (1,438,100)
Loss from continuing operations	$ (982,800)	$ (1,164,800)	$ (863,400)	$ (1,299,200)
Discontinued operations, net of tax	$ (277,600)	$ (439,300)	$ (745,800)	$ (475,800)
Net loss	$ (1,260,400)	$ (1,604,100)	$ (1,609,200)	$ (1,775,000)
Loss per share, basic				
Continuing operations	$ (0.07)	$ (0.09)	$ (0.07)	$ (0.10)
Discontinued operations	$ (0.02)	$ (0.03)	$ (0.06)	$ (0.04)
	$ (0.09)	$ (0.12)	$ (0.13)	$ (0.14)
Basic weighted average shares outstanding	14,023,456	13,490,917	12,873,194	12,319,657
Loss per share, diluted				
Continuing operations	$ (0.07)	$ (0.09)	$ (0.07)	$ (0.11)
Discontinued operations	$ (0.02)	$ (0.03)	$ (0.06)	$ (0.04)
	$ (0.09)	$ (0.12)	$ (0.13)	$ (0.14)
Diluted weighted average shares outstanding	14,023,456	13,490,917	12,873,194	12,319,657

N. SUBSEQUENT EVENTS

Entry into a Material Definitive Agreement – Plan and Agreement of Merger for Crested Corp.

On January 23, 2007, the Company and Crested signed a plan and agreement of merger (the "merger agreement") for the proposed acquisition of the minority shares of Crested (approximately 29.1%) not owned by the Company, and the subsequent merger of Crested into the Company pursuant to Wyoming and Colorado law (the Company is a Wyoming corporation and Crested is a Colorado corporation). The merger agreement was approved by all directors of both companies. The Company (and its officers and directors) have signed an agreement to vote its and their shares of the Crested in line with the vote of the holders of a majority of the Crested's minority shares. The affirmative vote of the holders of a majority of the Crested's outstanding shares is required to consummate the merger. The Company will not seek shareholder approval of the merger. Pursuant to the merger agreement, the Company will issue a total of approximately 2,802,481 shares of common stock to the minority holders of Crested common stock, including the shares equal to the equity value of options to buy the Crested's common stock underlying 1,700,000 options. (See Note C)

Entry into a Material Definitive Agreement – For Sale of Uranium Assets to sxr Uranium One Inc.

On February 22, 2007, the Company and Crested, and certain of their private subsidiary companies, signed an Asset Purchase Agreement (the "APA") with sxr Uranium One Inc. ("Uranium One," headquartered in Toronto, Canada with offices in South Africa and Australia (Toronto Stock Exchange and Johannesburg Stock Exchange, "SXR")), and certain of its private subsidiary companies.

The following is only a summary of the APA, and is qualified by reference to the complete agreement filed as an exhibit to this Report.

At closing of the APA, the Company and Crested will sell substantially all of their uranium assets (the Shootaring Canyon uranium mill in Utah, unpatented uranium claims in Wyoming, Colorado, Arizona and Utah (and geological library information related to the claims), and the Company's and Crested's contractual rights with Uranium Power Corp.), to subsidiaries of Uranium One, for consideration (purchase price) comprised of:

- $750,000 cash (paid in advance on July 13, 2006 after the parties signed the Exclusivity Agreement).
- 6,607,605 Uranium One common shares, at closing.
- Approximately $5,000,000 at closing, as a UPC-Related payment. On January 31, 2007, the Company, Crested, and Uranium Power Corp. ("UPC), amended their purchase and sale agreement for UPC to buy a 50% interest in certain of the Company's and Crested's mining properties (as well as the mining venture agreement between the Company and Crested, and UPC, to acquire and develop additional properties, and other agreements), to grant the Company and Crested the right to transfer several UPC agreements, including the right to receive all future payments there under from UPC ($4,100,000 cash plus 1,500,000 UPC common shares), to Uranium One. For information about the agreements with UPC, see below.

At closing of the APA, Uranium One will acquire the Company's and Crested's agreements with UPC (excluding those agreements related to Green River South, which will be retained by UPC), for which Uranium One will pay the Company and Crested the UPC-Related payment in an amount equal to a 5.25% annual discount rate applied to the sum of (i) $4,100,000 plus (ii) 1,500,000 multiplied by the volume weighted average closing price of UPC's shares for the 10 trading days ending five days before the APA is closed.

- Approximately $1,400,000, at closing, to reimburse the Company and Crested for uranium property exploration and acquisition expenditures from July 10, 2006 to the closing of the APA. These reimbursable costs relate to the Company's and Crested's expenditures on the properties being sold to Uranium One since the signing of the Exclusivity Agreement.

- Additional consideration, if and when certain events occur as follows:

    - $20,000,000 cash when commercial production occurs at the Shootaring Canyon Mill (when the Shootaring Canyon Mill has been operating at 60% or more of its design capacity of 750 short tons per day for 60 consecutive days).

    - $7,500,000 cash on the first delivery (after commercial production has occurred) of mineralized material from any of the properties being sold to Uranium One under the APA (excluding existing ore stockpiles on the properties).

    - From and after commercial production occurs at the Shootaring Canyon Mill, a production royalty (up to but not more than $12,500,000) equal to five percent of (i) the gross value of uranium and vanadium products produced at and sold from the mill; or (ii) mill fees received by Uranium One from third parties for custom milling or tolling arrangements, as applicable. If production is sold to a Uranium One affiliate, partner, or joint venturer, gross value shall be determined by reference to mining industry publications or data.

- Assumption of assumed liabilities: Uranium One will assume certain specific liabilities associated with the assets to be sold, including (but not limited to) those future reclamation liabilities associated with the Shootaring Canyon Mill in Utah, and the Sheep Mountain properties in Wyoming. Subject to regulatory approval of replacement bonds issued by a Uranium One subsidiary as the responsible party, cash bonds in the approximate amount of $6,883,300 on the Shootaring Canyon Mill and other reclamation cash bonds in the approximate amount of $413,400 will be released and the cash will be returned to the Company and Crested by the regulatory authorities. Receipt of these amounts is expected to follow closing of the APA.

All consideration will be paid to the Company, for itself and as agent for Crested and the several private subsidiaries of the Company and Crested that are parties to the APA. As of the date of this Report, the Company and Crested have not finalized the allocation of the consideration as between the Company and Crested and the subsidiaries.

Closing of the APA is subject to satisfaction of closing conditions customary to transactions of this nature, including (i) approval by the Toronto Stock Exchange of the issuance of the Uranium One common shares; (ii) approval by the State of Utah of the transfer to a Uranium One subsidiary of ownership of the Utah Department of Environmental Quality, Division of Radiation Control Radioactive Material License related to the Shootaring Canyon Mill; and (iii) the termination of the review period and receipt of a favorable ruling (following an 'Exon-Florio' filing to be made by the parties under the APA) that the transactions contemplated by the APA would not threaten the national security of the United States.

USECC holds a 4% net profits interest on Rio Tinto's Jackpot uranium property located on Green Mountain in Wyoming. This interest is not included in the APA.

The APA also provides that the Company, Crested and Uranium One will enter into a "strategic alliance" agreement at closing under which, for a period of two years, Uranium One will have the first opportunity to earn into or fund uranium property interests which may in the future be owned or acquired by the Company and Crested outside the five mile area surrounding the purchased properties.

InterWest

On January 8, 2007 InterWest, Inc. signed a Contract to Buy and Sell Real Estate to purchase approximately 10.15 acres of land located in Gillette, Wyoming. The purchase price is $1,268,800 payable as follows: $25,000 earnest money deposit and $1,243,800 payable at closing. InterWest has a sixty day due diligence period wherein it is to evaluate the property and obtain entitlements necessary to construct a 216 unit multifamily housing complex on the property. It is estimated that the construction cost of these rental units will be between $22 and $25 million. The Board of Directors has directed the management of InterWest that they should attempt to invest no more than 20% equity in the project should it go forward and that the balance of the funds must come from lenders. In the event that the entitlements do not prove up InterWest is not obligated to purchase the property.

SGMI Debt and Contingent Stock Purchase Warrant

On March 14, 2007, SGMI reached a Settlement Agreement with USE, Crested and USECC concerning: 1) an accumulated debt obligation by SGMI of approximately $2,025,700 for expenditures made by USECC on behalf of SGMI and 2) a Contingent Stock Purchase Warrant between SGMI, USE and Crested.

Pursuant to the terms and conditions of the Settlement Agreement, the parties agreed as follows:

1. To settle the accumulated debt obligation as of December 31, 2006 of $2,025,700, USECC agreed to accept 7,621,867 shares of SGMI common stock (subject to approval by the Toronto Stock Exchange ("Exchange")). The debt is therefore being paid at negotiated price of $.26 per share. The price for SMGI stock on March 15, 2007 was $.20 per share.

2. To settle the Contingent Stock Purchase Warrant agreement of approximately $4.6 million, USE and Crested agreed to accept a 5% net profits interest royalty ("NPIR") in exchange for the Contingent Stock Purchase Warrant. Furthermore, USE and Crested agree that the 5% royalty shall continue until USE and Crested have recouped the $4.6 million. Once the $4.6 million is recouped the 5% NPIR shall be converted to a 1% NPIR thereafter.

3. In addition, subject to the closing of USE and Crested's sxr Uranium One transaction, USE and Crested have agreed to provide a $1 million line of credit ($500,000 each) to SGMI at 12% annual interest, drawable and repayable at anytime in tranches of $50,000 or more by SGMI. USE and Crested have the sole option to have SGMI repay the debt in cash or SGMI stock at a 10% discount to the 10 day VWAP before payment (subject to Exchange approval).

OFFICERS AND DIRECTORS

Keith G. Larsen
Chairman, CEO
Director
(a, b-alternate, c)

Mark J. Larsen
President, COO, Director
(a)

Harold F. Herron
Sr. Vice President, Director
(a, c)

R. Scott Lorimer
V.P. Finance, CFO,
Treasurer and Controller

Steven Youngbauer
General Counsel

Michael H. Feinstein
Financial and Business
Consultant, Director
(b, d, e)

Michael T. Anderson
CFO for Natchez Regional
Medical Center, Director
(b, d, e)

Allen S. Winters
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and former V.P. / General
Manager for Homestake
Mining Co., Director
(b, d)

H. Russell Fraser
Former President and
Director of American
Capital Access, Inc.,
Director
(a, b, d, e)

(a) Executive committee member
(b) Audit committee member
(c) ESOP trustee
(d) Compensation committee member
(e) Nominating committee member

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Stock Trading

The Company's Common Stock is traded on the NASDAQ Capital Market under the trading symbol USEG.

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