

properties. All of its mineral properties are undeveloped and require significant capital expenditures before any commercial operations are commenced. The Company has operations in both the United States and Saudi Arabia. The Company's undeveloped mineral interests are primarily located in Saudi Arabia.

The Company, through its indirect wholly owned subsidiary, South Hampton Refining Company ("South Hampton"), owns and operates a specialty products refinery which is the Company's only significant revenue producing asset.

The Company holds a mining lease covering a 44 square kilometer area in the Al Masane area in southwestern Saudi Arabia. In a 1996 update to the 1994 full bank feasibility study of the Al Masane lease area conducted by an independent mining consulting firm, the consultants estimate the total capital costs of the Al Masane project to be \$88.6 million. The Company and its Saudi Arabian advisors are in the process of forming a Saudi limited liability company to own and operate the project. On November 5, 1997, the Company and the Al Mashreq Company for Mining Investments ("Al Mashreq"), a Saudi limited liability company owned by Saudi Arabian investors, initialed a joint venture agreement to form a Saudi limited liability company which will be owned 50% by the Company and 50% by Al Mashreq. The new company, called "The Arabian Shield Company for Mining Industries Ltd.", is now under formation, and has applied to the Saudi Ministry of Commerce for a charter to operate the mine. The Company is diligently pursuing the financing of the project so that commercial production can begin as contemplated in the updated feasibility study. There can be no assurance that adequate capital for the project can be obtained in order for commercial production to begin as contemplated. The ultimate recovery of mineral exploration and development costs of the Company's other mineral properties cannot presently be determined.

Saudi Arabian Activities. On May 22, 1993, the Company was granted a 30-year mining lease covering a 44 square kilometer area in the Al Masane area in southwestern Saudi Arabia.

The Company was granted exploration licenses for the Wadi Qatan and Jebel Harr areas in southwestern Saudi Arabia, approximately 30 kilometers east of the Al Masane area, in 1971 and 1977, respectively. The exploration licenses by their terms have expired, and although Saudi Arabian government officials have orally advised the Company that the licenses will be extended as long as mineral exploration is being carried out on the areas which they cover, formal extensions from the government have not been obtained and there can be no assurance that the Company's license rights will be honored. The Company remains a party to an agreement with the Petroleum and Mineral Organization ("Petromin"), the official mining and petroleum company of the Saudi Arabian government, which governs the rights of the parties if an exploration license is converted into a mining lease. When financing for the Al Masane project is completed, the Company plans to make an application for an expanded exploration license for an area of approximately 2,800 square kilometers which includes the original Greater Al Masane area and the Wadi Qatan and Jebel Herr areas. See Item 2. Properties.

-1-

In May 1993, the Company had discussions with Chevron Chemical Company regarding the Company's proposal to purchase 5,000 barrels per day of mixed pentanes from an Aromax(R) petrochemical project to be built in Jubail, Saudi Arabia by Chevron Chemical in a joint venture with Saudi Venture Capital Group (SVCS). The Company and some Saudi partners, all of whom are directors and/or stockholders of the Company, plan to form a Saudi limited liability company which will build and manage a processing plant located next to the Aromax(R) plant in Saudi Arabia. The Company would have a 25% interest in the limited liability company and would manage the plant. The plant will be similar to the South Hampton refinery in producing purified pentanes from a feedstock of mixed pentanes obtained from the Aromax(R) plant. Chevron Chemical advised the Company by letter in July 1993 that Chevron Chemical and SVCS jointly agreed to commit to supply the proposed pentane project with up to 5,000 barrels per day of mixed pentane feedstock. Engineering and marketing studies of the project made in 1994 by outside consultants reflected positive results. Planning then began toward the construction and operation of the Aromax(R) plant. The Aromax(R) plant received final approval from the Saudi Arabian government in March 1996 and Chevron Chemical began construction soon thereafter. The source of feedstock supply to the Aromax(R) plant has changed resulting in Chevron Chemical and SVCS being unable to supply the proposed processing plant. The Company has held discussions with several Saudi Arabian companies regarding feedstock and transportation arrangements, although there can be no assurances that any such arrangements can be made. The Company applied for and received a license to build the proposed processing plant and further planning and design work are underway.

In December 1993, the Company commissioned Sherritt Ltd. of Fort Saskatchewan, Canada, to prepare a conceptual engineering design for a proposed zinc refinery based on Sherritt's two stage pressure leach process, to be built by the Company and Saudi partners at the Red Sea port of Yanbu, Saudi Arabia. The refinery would have the capacity to produce 100,000 tonnes of slab zinc per

year, with elemental sulfur as a by-product. Sherritt Ltd. completed the study in May 1994 which contains a proposed flow sheet that has been commercialized and designed for a state of the art zinc refinery. Sherritt's zinc pressure leach technology provides significant advantages over other existing zinc production processes, including having the reputation as the most favored technology for environmental considerations. In its study, Sherritt concluded, after considering all of the presently identifiable elements, that they offer a strong potential for the project and enhance the concept. Sherritt encouraged the Company to carry out further studies toward the implementation of the project. There has been a recent inquiry about this project from a zinc smelting and refining company in Asia.

United States Activities. The Company has two direct wholly owned subsidiaries, American Shield Refining Company (the "Refining Company") and American Shield Coal Company (the "Coal Company"). The Refining Company owns all of the capital stock of Texas Oil and Chemical Co. II, Inc. ("TOCCO"). TOCCO owns all of the capital stock of South Hampton, and South Hampton owns all of the capital stock of Gulf State Pipe Line Company, Inc. ("Gulf State"). South Hampton owns and operates a special products refinery near Silsbee, Texas. Gulf State owns and operates three pipelines which connect the South Hampton refinery to a natural gas line, to South Hampton's truck and rail loading terminal and to a marine terminal owned by an unaffiliated third party. The Company also beneficially owns approximately 52%, and directly owns approximately 44%, of the capital stock of an inactive Nevada mining company, Pioche-Ely Valley Mines, Inc. ("Pioche").

Al Masane Project

Prior Feasibility Studies. In the years following the granting of the exploration licenses in August 1971, substantial geological and geophysical work was accomplished on the Al Masane and Wadi Qatan license areas. Core drilling on the licensed areas and studies conducted by independent consulting firms indicated that the copper, zinc, gold and silver prospects at Al Masane had a chance of being put into production sooner than the nickel prospect at Wadi Qatan. Metallurgical tests also showed difficulty in separating the nickel at Wadi Qatan. During 1977, a

-2-

pre-feasibility mining study was conducted at Al Masane by the mining consulting firm of Watts, Griffis and McQuat Limited of Toronto, Canada ("WGM"). WGM concluded that the Al Masane prospect should be further developed and recommended an extensive development program for the area.

Phase I of the development program recommended by WGM for Al Masane was completed in April 1981 and involved underground development in the form of a decline (700 meters) and tunnels (3,100 meters) parallel to the ore bodies from where extensive underground core drilling was done to prove the ore reserves. The project was financed for the most part with an \$11 million interest-free loan from the Saudi Arabian government (Ministry of Finance). After completion of Phase I, the Company's consultants concluded that sufficient ore reserves had been established to justify a full bank feasibility study to determine the economic potential of establishing a commercial mining and ore treatment operation at Al Masane. The study was conducted principally by WGM, assisted by SNC/GECO of Montreal, Canada in engineering and costing. The consultants concluded in their 1982 study that the Al Masane deposits would support commercial production of copper, zinc, gold and silver and recommended implementation of Phase II of the Al Masane development program, which involves the construction of mining, ore treatment and support facilities. WGM reevaluated the Al Masane project in September 1984 and concluded that the cumulative effect of the factors considered in the reevaluation was positive.

Additional exploration work conducted at Al Masane and substantial changes in metal prices and capital and operating costs occurring since 1984 led the Company to request WGM to reevaluate the project in early 1989. The additional exploration occurring after 1984 in the Al Houra and Moyeath zones resulted in a better definition of and addition to these zones. Consequently, the consultants revised their reserve estimates. Some of the reserves previously defined as possible were reclassified as proven or probable. Based on its reevaluation of the Al Masane project, WGM again concluded that under the most realistic scenarios the proposed mining operation was economically viable and had the potential to provide a satisfactory return on investment.

In May 1992, WGM, at the Company's request, revised its cash flow projections for the Al Masane project based on then current metal prices. The cash flow projections were positive.

In both the 1989 reevaluation and the 1992 cash flow projections, WGM continued to regard Al Masane as having high potential for the discovery of additional ore zones.

1994 Feasibility Study. Following the granting of the mining lease to the Al Masane area on May 22, 1993, the Company commissioned WGM to prepare a new fully bankable feasibility study for presentation to financial institutions in connection with obtaining financing for the project. The feasibility study includes more metallurgical work incorporating advances in grinding of the ore; incorporation of the latest advances in technology and reagents developed

during the past ten years; incorporation of new mill designs and the latest water recycling methods; investigation into the shipping and marketing of zinc and copper concentrates; and an economic analysis of the project. The feasibility study contains specific recommendations to insure that the construction of the project is accomplished as expeditiously and economically as possible. Engineering design and costing of the project was done by Davy International of Toronto, Canada. The feasibility study cost the Company approximately \$1 million and was presented to the Company on July 22, 1994.

The Al Masane ore is located in three mineralized zones known as Saadah, Al Houra and Moyeath. The following table sets forth a summary of the diluted minable, proven and probable ore reserves at the Al Masane project, along with the estimated average grades of these reserves:

-3-

<TABLE>
<CAPTION>

Zone	Reserve (Tonnes)	Copper (%)	Zinc (%)	Gold (g/t)	Silver (g/t)
<S> Saadah	<C> 3,872,400	<C> 1.67	<C> 4.73	<C> 1.00	<C> 28.36
Al Houra	2,465,230	1.22	4.95	1.46	50.06
Moyeath	874,370	0.88	8.92	1.29	64.85
Total	7,212,000	1.42	5.31	1.19	40.20

</TABLE>

For purposes of calculating, proven and probable reserves, a dilution of 5% at zero grade on the Saadah zone and 15% at zero grade on the Al Houra and Moyeath zones was assumed. A mining recovery of 80% has been used for the Saadah zone and 88% for the Al Houra and Moyeath zones. Mining dilution is the amount of wallrock adjacent to the ore body which is included in the ore extraction process.

Proven reserves are those mineral deposits for which quantity is computed from dimensions revealed in outcrops, trenches, workings or drillholes, and grade is computed from results of detailed sampling. For ore deposits to be proven, the sites for inspection, sampling and measurement must be spaced so closely and the geologic character must be so well defined that the size, shape, depth and mineral content of reserves are well established. Probable reserves are those for which quantity and grade are computed from information similar to that used for proven reserves, but the sites for inspection, sampling and measurement are farther apart or are otherwise less adequately spaced. However, the degree of assurance, although lower than that for proven reserves, must be high enough to assume continuity between points of observation.

A review by WGM of the equipment and process flowsheet contained in the 1982 feasibility study prepared by WGM indicated that new technology developed during the past ten years could be used to reduce the capital cost and improve the metallurgical recoveries. In particular, the use of semi-autogenous grinding to reduce the capital cost of the grinding section and developments in reagents were believed to hold the greatest potential for improving the economies of the project. A detailed metallurgical testwork program was undertaken by Lakefield Research in 1994 to address potential improvements and provide detailed design criteria for the concentrator design. Results from this testwork program showed that copper recovery could be improved by 5.7% and zinc recoveries improved by 13% compared to the 1982 results.

The metallurgical studies conducted on the ore samples taken from the zones indicated that 87.7% of the copper and 82.6% of the zinc could be recovered in copper and zinc concentrates. Overall, gold and silver recovery from the ore was estimated to be 77.3% and 81.3%, respectively, partly into copper concentrate and partly as bullion through cyanide processing of zinc concentrates and mine tailings.

A test program to evaluate the economies of the cyanidation of the zinc concentrate and tailings in order to improve gold and silver recoveries found gold and silver recoveries to range from 50% to 77%. To recover gold and silver from the zinc concentrate and tailings, WGM recommended that a cyanidation plant be included in the process flowsheet. Dore bullion would be produced. WGM concluded that the inclusion of a cyanidation plant would make a positive contribution to the economies of the project under the base conditions.

The mining and milling operation recommended by WGM for Al Masane would involve the production of 2,000 tonnes of ore per day (700,000 tonnes per year), with a mine life of over ten years. Annual production is estimated to be 34,900 tonnes of copper concentrate (25% copper per tonne) containing

precious metal and 58,000 tonnes of zinc concentrate (54% zinc per tonne). Total output per year of gold and silver is estimated to be 22,000

-4-

ounces of gold and 800,000 ounces of silver from the copper concentrate and bullion produced. The construction of mining, milling and infrastructure facilities is estimated to take 18 months to complete. Construction necessary to bring the Al Masane project into production includes the construction of a 2,000 tonne per day concentrator, infrastructure with a 300 man housing facility and the installation of a cyanidation plant to increase the recovery of precious metals from the deposit. Project power requirements will be met by diesel generated power.

WGM recommended that the Al Masane reserves be mined by underground methods using trackless mining equipment. Once the raw ore is mined, it would be subjected to a grinding and treating process resulting in three products to be delivered to smelters for further refining. These products are zinc concentrate, copper concentrate and dore bullion. The copper concentrate will contain valuable amounts of gold and silver. These concentrates are estimated to be 22,000 ounces of gold and 800,000 ounces of silver and will be sold to copper and zinc custom smelters and refineries worldwide. After smelter refining process, the metals could be sold by the Company or the smelter for the Company's account in the open market.

WGM prepared an economic analysis of the project utilizing cash flow projections. In the feasibility study, WGM recommends that the Company bring the Al Masane mine into production.

In the feasibility study, WGM states that there is potential to find more reserves within the lease area, as the ore zones are all open at depth. Further diamond drilling, which will be undertaken by the Company, is required to quantify the additional mineralization associated with these zones. A significant feature of the Al Masane ore zones is that they tend to have a much greater vertical plunge than strike length; relatively small surface exposures such as the Moyeath zone are being developed into sizeable ore tonnages by thorough and systematic exploration. Similarly, systematic prospecting of the small gossans in the area could yield significant tonnages of new ore.

1996 Update. The Company requested WGM and Davy International to update the 1994 feasibility study of the project. The update details various changes required to update the 1994 feasibility study to reflect costs as of the first quarter of 1996. Capital and operating cost updates to the surface infrastructure and mill components were done by Davy International of Toronto, Canada. WGM was responsible for updating mining, mining related activities and an economic analysis.

The 1996 update shows the estimated capital cost to bring the project into operation to be \$88.6 million, a 9% increase over the \$81.3 million capital cost estimated in the 1994 feasibility study. At a production rate of 700,000 tonnes per year, the operating cost of the project (excluding concentrate freight, ship loading, smelter charges, depreciation, interests and taxes) was estimated to be \$38.49 per tonne of ore milled compared to \$36.86 per tonne of ore milled estimated in the 1994 feasibility study.

WGM prepared an economic analysis of the project utilizing cash flow projections. A base case was prepared that included those project elements which are most likely to be achieved. WGM believed that a majority of the base case assumptions used in the 1994 feasibility study remained valid, including the ore reserves, mill feed grade, production rate, metal recoveries and concentrate grade and smelter returns. Metal prices, capital costs, operating costs and the corporate structure were adjusted to reflect more current information. Capital and operating costs were adjusted in conformity with the updated estimates prepared by Davy International.

The base case assumes the corporate structure of the entity to be formed to operate the project, currently planned to be a Saudi limited liability company, will be owned 50% by the Company and 50% by Saudi Arabian investors and that the owners of this entity would contribute an aggregate of \$21.2 million to the cost of the project. The base case further assumes financing for the project from commercial loans in the aggregate amount of \$21.2 million bearing interest at the rate of 8% per year and a loan in the amount of \$43.8 million from the Saudi Industrial Development Fund ("SIDF") repayable in equal annual installments over the initial life of the mine. The remainder of the project financing would be contributed by cash generated by the operation of the project. The base case assumes that the \$11 million loan outstanding to the Saudi Arabian government will be paid by the Company in accordance with a repayment schedule to be agreed upon with the Saudi Arabian government from the Company's share of the project's cash flows. Based on these assumptions, and assuming the average prices of metal over the life of the mine to be \$1.05 per pound for copper,

-5-

\$.60 per pound for zinc, \$400 per ounce of gold and \$6.00 per ounce of silver, WGM's economic analysis of the base case shows the project will realize an internal rate of return of 13.1%, the Company's and the Saudi Arabian investors' internal rates of return would be 27.3% and 12.1%, respectively, and projected net cash flow from the project of \$95.1 million. The 1994 feasibility study base case showed the project would realize a 14.05% internal rate of return. Cash flow under the base case is exclusive of income tax as the base case assumes that any such tax would be paid by individual investors and not by the project. Assuming a 10% discount rate, the net present value of the project as shown in the update is \$12.16 million compared to the \$15.5 million net present value of the project shown in the 1994 feasibility study. Based on the update, WGM believes that the economic analysis shows that the project remains viable.

Project Financing and Mining Lease. The 1996 update to the 1994 feasibility study shows the estimated total capital cost to bring the Al Masane project into production to be \$88.6 million. At the present time, the Company does not have sufficient funds to bring the project into production. The Company and its Saudi Arabian advisors are in the process of forming a Saudi limited liability company to own and operate the project. On November 5, 1997, the Company and Al Mashreq initialed a joint venture agreement to form a Saudi limited liability company which will be owned 50% by the Company and 50% by Al Mashreq. The new company, called "The Arabian Shield Company for Mining Industries Ltd.", is now under formation, and has applied to the Saudi Ministry of Commerce for a charter to operate the mine.

On May 20, 1996, the Company entered into a Financial and Legal Services and Advice Agreement with Nasir Ali Kadasah, for legal advice, and Dar Al Khaleej, for research and economic advice. The purpose of this agreement was for the two Saudi Arabian advisors to assist the Company in obtaining financing for the Al Masane project. To this end, the agreement contemplated that the Saudi Arabian advisors would perform the following:

1. The formation of a Saudi limited liability company, 50% of which would be owned by the Company and the remaining 50% of which would be owned by Saudi Arabian investors who will contribute 25% of the total capital cost of the project.
2. Obtain an industrial license for the project from The Ministry of Industry and Electricity. This license was a necessary prerequisite for obtaining an interest-free loan from the SIDF to fund 50% of the capital cost of the project.
3. Finalize the necessary procedures to obtain such loan from the SIDF, the application for which was submitted on September 30, 1995.
4. Apply for and receive loans from commercial banks necessary to finance the project.
5. Apply for and obtain the Ministerial Resolution from the Minister of Petroleum and Mineral Resources approving the transfer of the mining lease to the Saudi limited liability company.

The agreement provided that the Saudi Arabian advisors would be solely responsible for the performance of the foregoing obligations and that the Company had no obligation therefor.

As consideration for performing these obligations, the Company agreed to pay Mr. Kadasah and Dar Al Khaleej \$10,000 each upon the issuance of the industrial license and Mr. Kadasah \$10,000 upon approval of the loan by the SIDF. The Company also agreed to issue to Mr. Kadasah and Mr. Tawfiq Abdulaziz Al-Sowailim, as agent for Dar Al Khaleej, up to 1,025,000 and 975,000 shares of the Company's Common Stock, respectively, and to grant Mr. Kadasah and Mr. Tawfiq Abdulaziz Al-Sowailim, as agent for Dar Al Khaleej, options to purchase up to 1,425,000 and 875,000 shares of the Company's Common Stock, respectively. The Company was obligated to issue

-6-

such shares and grant such options in designated amounts upon completion of each of the foregoing obligations. The issuance of the shares would be for consideration consisting solely of services rendered to the Company. The options are immediately exercisable on the date of grant, have a five-year term commencing on the date of formation of the Saudi limited liability company and an exercise price of \$1.00 per share. On December 3, 1996, the industrial license was issued to the Company and its Saudi Arabian advisors. As a result, the Company paid the advisors \$20,000 in the aggregate and was obligated at December 31, 1997 to issue to these advisors 300,000 shares of the Company's Common Stock in the aggregate and options to purchase 345,000 shares of the Company's Common Stock in the aggregate having an exercise price of \$1.00 per share. The agreement was terminated in August 1997 and negotiations are being held to complete a new agreement, although there can be no assurances that any such agreement can be reached.

A loan application was submitted to SIDF on September 30, 1995 and conditional approval was received on December 17, 1997 for a \$38.08 million loan. The SIDF makes interest-free loans to industrial projects in Saudi Arabia

and charges a 2.5% service fee. The Company believes that it may also be able to finance the remaining cost of the project through arrangements with suppliers and equipment manufacturers, custom smelters and additional debt or equity financing secured by the Company, however, there can be no assurances to that effect.

The joint venture agreement with Al Mashreq contemplates the formation of a new Saudi limited liability company, "The Arabian Shield Company for Mining Industries Ltd.", to be owned 50% by the Company and 50% by Al Mashreq. As contemplated, the Saudi limited liability company will be responsible for the construction and operation of the mining facilities. Title to the mining lease would be transferred to the Saudi limited liability company. The joint venture agreement further contemplates the Company transferring its beneficial interest in the Al Masane project to the Saudi limited liability company when title to the mining lease is transferred to the Saudi limited liability company. The Company and Al Mashreq agree to attempt to obtain financing for the project, and that if firm commitments for such financing on acceptable terms are not obtained by November 5, 1998, either party may terminate the agreement without liability, except that the Company will return to Al Mashreq any consideration paid for the assignment of the beneficial interest in the project and full title to the mining lease will revert to the Company.

Pursuant to the mining lease agreement, when the profitability of the project is established, the Company is obligated to form a Saudi public stock company with Petromin. It is contemplated that the Saudi limited liability company then will be transformed into a Saudi public stock company, that the Company and Al Mashreq will own no less than 50% of the shares of the Saudi public stock company, that Petromin will have an option to acquire up to 25% of the shares and that the remaining shares will be offered for sale in Saudi Arabia pursuant to a public subscription. Title to the mining lease and the other obligations specified in the mining lease will be transferred to the Saudi public stock company. Responsibility for the repayment of the \$11 million loan from the Saudi Arabian government will remain with the Company. In December 1994, the Company received instructions from the office of the Minister of Petroleum and Mineral Resources stating that it is possible for the Company to form the Saudi public stock company without Petromin but that the sale of stock to the Saudi public could occur only after two years of profits from commercial operations of the mine. The instructions added that Petromin will still have the right to purchase shares in the Saudi public stock company any time it desires.

As the holder of the Al Masane mining lease, the Company is solely responsible to the Saudi Arabian government for the rental payments and other obligations provided for by the mining lease and repayment of the \$11 million loan secured by the Company from the Saudi Arabian government. The mining lease provides that the Company intends to repay the loan in accordance with a repayment schedule to be agreed upon with the Saudi Arabian government from its share of project cash flows. The initial term of the lease is for a period of thirty (30) years from May 22, 1993, with the Company having the option to renew or extend the term of the lease for additional periods not to exceed twenty (20) years. Under the lease, the Company agreed to pay in advance a surface rental at the rate of ten thousand Saudi Riyals (approximately \$2,667 at the current exchange rate) per square kilometer per year (approximately \$117,300 annually) during the period of the lease. The Company has made all rental payments under the

-7-

lease. It is contemplated that responsibility for the payment of all future rental payments would be assumed by the Saudi limited liability company when title to the Al Masane mining lease is transferred to it. In addition, the Company must pay income tax in accordance with the income tax laws of Saudi Arabia then in force and pay all infrastructure costs. Under the Saudi Arabian Mining Code, income tax will not be due during the first stage of mining operations, which is the period of five years starting from the earlier of (i) the date of the first sale of products or (ii) the beginning of the fourth year since the issue of the mining lease. The lease gives the Saudi Arabian government priority to purchase the Company's whole production of gold or any part thereof from the project. The lease also gives the Saudi Arabian government the right to purchase up to 10% of the Company's annual production of other minerals on the same terms and conditions then available to other similar buyers and at current prices then prevailing in the free market. The lease contains provisions requiring that preference be given to Saudi Arabian suppliers and contractors and that the Company employ Saudi Arabian citizens and provide training to Saudi Arabian personnel.

Reference is made to the map on page 13 of this Report for information concerning the location of the Al Masane project.

Other Exploration Areas in Saudi Arabia

During the course of the exploration and development of the Al Masane area, the Company has carried on exploration work in other areas in Saudi Arabia and is planning to apply for an additional exploration license for these areas. With respect to these other areas, the Company has an agreement with Petromin which governs the rights of the parties if the exploration licenses granted to the Company are converted into a mining lease. Under this

agreement, Petromin is granted an option to acquire, at any time, a 25% interest in any project to mine minerals in Saudi Arabia the exploration for which has been conducted under the exploration licenses.

U.S. Mineral Interests

The Company's mineral interests in the United States include its equity interest in the Coal Company and Pioche. The Coal Company no longer owns or holds any mineral interests and is presently inactive. The future of the Coal Company's operations is uncertain. Pioche has been inactive for many years, but in October 1997, Pioche entered into an Exploration Agreement and Option to Purchase with a large mining company which provides for annual payments to Pioche of \$50,000 for seven years until, or unless, the mining company exercises an option to purchase an 85% interest in the mining claims for \$3 million. The agreement can be terminated upon 60 days written notice by the mining company. The mining company has agreed to expend at least \$50,000 in exploration work each year and to drill at least one hole in the first year.

Special Products Refinery

South Hampton owns and operates a special products refinery near Silsbee, Texas and currently employs 50 people. The refinery is presently devoted to specialized processing activities. The refinery currently consists of seven operating units which, while interconnected, make distinct products through differing processes: (i) a pentane-hexane unit; (ii) a catalytic reformer; (iii) an aromatics hydrotreating and fractionation unit; (iv) a cyclopentane unit; (v) an Aromax(R) unit; (vi) an aldehyde hydrogenation unit; and (vii) a specialty fractionation unit. All of these units are presently in operation.

The design capacity of the pentane-hexane unit is approximately 2,200 BPD of feedstock. The unit averaged 1,945 barrels per stream day during 1997. The unit consists of a series of fractionation towers and hydrotreaters capable of producing high purity solvents which are sold primarily to expandable polystyrene and high density polyethylene producers. South Hampton purchases most of its feedstock for this unit on the spot market.

-8-

The catalytic reforming unit is a standard industry design using platinum-rhenium catalyst which produces an aromatics concentrate used as feedstock for an aromatics extraction unit, as well as hydrogen which is utilized in other processes. The design capacity of the reformer is 4,000 BPD. The unit is operated as a source of hydrogen for the pentane-hexane unit and operates in tandem with the Aromax(R) unit as feedstock balances dictate. The unit averaged 417 barrels per stream day during 1997.

The aromatics hydrotreating and fractionation unit consists of a hydrotreating reactor and a single fractionation tower and has a design capacity of 500 BPD. By-product chemical streams have historically been processed by this unit into two products, high octane gasoline blendstocks and heavy aromatic oils sold as fuel oil blending stock. This unit is leased to a customer for its own use pursuant to a contract providing for the payment of a minimum daily charge.

The cyclopentane unit consists of three specialized fractionation towers designed to produce a consistently high quality product which is used in the expandable polystyrene industry. The design capacity of the cyclopentane unit is 400 BPD. The unit operates according to the feedstock supplied by the pentane-hexane unit and averaged 192 barrels per stream day during 1997.

The Aromax(R) unit is the world's first commercial unit using a proprietary process of Chevron Research Company to produce a high benzene content product which is sold as feedstock to refiners operating benzene extraction units. The process converts petroleum naphtha into liquid hydrocarbons having a higher aromatic hydrocarbon content. The aromax unit capacity is 400 BPD and uses a by-product of the pentane-hexane unit as feedstock. The unit operates according to the feedstock supplied from the pentane-hexane unit and the other hydrotreaters. The unit averaged throughput of 122 barrels per stream day during 1997. Chevron Research has agreed to continue development of the Aromax(R) process. The unit has continued to successfully operate as designed.

The specialty fractionation unit consists of two fractionation towers and has a design capacity of 1,000 BPD. This unit is leased to a customer for its own use pursuant to a contract providing for the payment of a minimum daily charge.

South Hampton also owns approximately 70 storage tanks with a total capacity of approximately 250,000 barrels. The refinery is situated on 100 acres of land, approximately 70 acres of which is developed. South Hampton owns a truck and railroad loading terminal consisting of eight storage tanks, a rail spur and truck and tank car loading facilities.

As a result of an expansion program of the production capacity of the South Hampton refinery completed in 1990, essentially all of the standing equipment at South Hampton is operational. The Company has surplus equipment

in storage on site with which to assemble further processing units, such as a hydrocracking unit with a 2,000 BPD capacity.

Gulf State owns and operates three 8" pipelines aggregating approximately 50 miles in length which connect the South Hampton refinery to a natural gas line, to South Hampton's truck and rail loading terminal and to a marine terminal owned by an unaffiliated third party. South Hampton leases storage facilities at the marine terminal.

Revenues and Financing

The Company's revenues and cash flows have been insufficient to meet its debt service and capital expenditure requirements. Accordingly, it has been necessary for the Company continually to seek additional debt and equity financing in order to have funds to continue development and other investing activities.

In 1995, the Company (i) negotiated an extension until April 30, 1996 of the maturity of the Amended and Restated Credit Agreement with Den norske Bank AS, (ii) borrowed \$721,000 in the aggregate from four individuals, including a stockholder of the Company who is the Vice Chairman of National Mining Company, a stockholder of

-9-

the Company, the President and Chief Executive Officer of the Company and a relative of such executive officer, pursuant to loans payable on demand two years after their issuance bearing interest at LIBOR plus 2%, such lenders having the option for a period of five years from the date of the loan to convert the principal amount of the loan and all accrued interest into shares of the Company's Common Stock at the rate of \$1.00 per share, (iii) received \$50,000 payment on a stockholder receivable from a 1993 sale of shares of its Common Stock to a private Saudi company controlled by a director and (iv) granted the President and Chief Executive Officer of the Company an option to convert at any time \$400,000 of deferred compensation for services rendered to the Company into shares of the Company's Common Stock at the rate of \$1.00 per share.

In 1996, the Company (i) through South Hampton negotiated an Amended and Restated Credit Agreement with Den norske Bank ASA, amending and restating the then outstanding credit agreement to provide for a revolving credit facility in an aggregate principal amount of up to \$1,965,000, (ii) restructured certain indebtedness of South Hampton owed to Saudi Fal Co., Ltd., a limited liability company owned by a stockholder of the Company ("Saudi Fal"), and the Refining Company pursuant to promissory notes in the original principal amounts of \$1,945,773.49 and \$1,694,605.08, respectively, which promissory notes are subordinated to the Amended and Restated Credit Agreement with Den norske Bank ASA, (iii) approved the sale of up to 1 million shares of the Company's Common Stock through private placements at a price no less than \$1.00 per share, (iv) sold 450,000 shares of the Company's Common Stock at \$1.00 per share to a Saudi Arabian investor who is a stockholder of the Company and approved the sale of an additional 450,000 shares of the Company's Common Stock at \$1.00 per share to the same investor, the purchase price for such additional shares being payable in monthly installments of \$100,000 and (v) approved the sale of 50,000 shares of the Company's Common Stock to a Saudi Arabian investor.

During 1997, the Company took certain actions designed to generate additional equity capital and improve its financial condition, including: (i) approval by the Company's Board of Directors in August 1997 of the sale of up to 1 million shares of the Company's Common Stock through private placements at a price no less than \$1.00 per share; (ii) the sale of 450,000 shares of the Company's Common Stock at \$1.00 per share to a Saudi Arabian investor who is a stockholder of the Company; (iii) the sale of 50,000 shares of the Company's Common Stock at \$1.00 per share to a Saudi Arabian investor; (iv) the issuance of 10,000 shares of its Common Stock at \$1.375 per share pursuant to an option exercise by an officer of the Company; (v) the issuance of 345,000 shares of its Common Stock in exchange for the cancellation of certain indebtedness; (vi) borrowing \$200,000 from a Saudi Arabian investor pursuant to a two-year demand promissory note bearing interest at prime plus 2% per annum; (vii) the sale by South Hampton Refining Company, an indirect, wholly owned subsidiary of the Company ("South Hampton"), in June 1997 of an office building to a third party for approximately \$695,000, on terms which included a ten-year promissory note having a principal amount of \$610,000 and bearing interest at 9% per annum; and (viii) receiving conditional approval for a \$38.08 million loan from the SIDF.

It may be necessary to secure funds to continue operations through the sale of portions of the Company's properties, its investments or a portion of the Company's interest therein. There are no assurances that these sales could be arranged or that sufficient additional equity or debt financing can be obtained.

On October 15, 1996, South Hampton entered into an Amended and Restated Credit Agreement (the "Credit Agreement") with Den norske Bank ASA (the "Bank"), amending and restating the then outstanding credit agreement to provide for a revolving loan facility in an aggregate principal amount of up to

\$1,965,000. The Bank's commitment to make funds available under the credit facility will be reduced by (i) \$75,000 on the last day of each fiscal quarter commencing December 31, 1996 and (ii) the amount of any distribution by South Hampton to Saudi Fal, the Company, the Refining Company or TOCCO in excess of amounts permitted under the Credit Agreement. Advances under the Credit Agreement may not at any time exceed the lesser of the commitment or a borrowing base calculated based upon the cash collateral account, eligible accounts receivable and inventory. Interest is payable monthly in arrears on all outstanding advances under the credit facility at the Bank's prime lending rate, as in effect from time to time, plus 1%. Principal and accrued and unpaid interest was payable on December 31, 1998, but in March 1998 the maturity date was extended to December 31, 1999. Subject to certain conditions and South Hampton maintaining various financial covenants and ratios, the Credit Agreement permits South Hampton to make distributions to (i) Saudi Fal, the Company, the Refining Company and TOCCO for legal, auditing and accounting fees attributable to the operations of South Hampton in an annual aggregate amount not in excess of \$60,000, (ii) Saudi Fal and the Company in respect of accrued interest on any debt owned by South

-10-

Hampton to Saudi Fal or the Company in an amount not in excess of \$17,500 per month and (iii) Saudi Fal and the Company in respect of principal on any debt owed by South Hampton to Saudi Fal or the Company. The Credit Agreement is secured by all of the assets of South Hampton and Gulf State and all of the issued and outstanding shares of TOCCO, South Hampton and Gulf State. South Hampton is required to collect all receivables through a cash collateral account at a local bank.

In connection with South Hampton's entry into the Credit Agreement with the Bank, South Hampton issued a Second Lien Promissory Note to Saudi Fal and a Third Lien Promissory Note to the Refining Company in the original principal amounts of \$1,945,773.49 and \$1,694,605.08, respectively, evidencing certain indebtedness of South Hampton owed to such parties. The promissory notes bear interest at the Bank's prime lending rate, as in effect from time to time, plus 1%. Interest only is due and payable monthly on the promissory notes, and the entire unpaid balance of principal and accrued and unpaid interest was due on December 31, 1998, but in March 1998 the maturity date was extended to December 31, 1999. The promissory notes are secured by all of the assets of South Hampton and Gulf State. The promissory notes and related liens are subordinated to the Credit Agreement. The promissory note issued to the Refining Company and related liens are subordinate to the promissory note issued to Saudi Fal.

The refinery had operating income of approximately \$1,868,000, before depreciation and amortization of approximately \$420,000, on gross refined product sales of approximately \$25,600,000 for the 1997 fiscal year compared with operating income of approximately \$655,000, before depreciation and amortization of approximately \$413,000, on gross refined product sales of approximately \$21,367,000 for the 1996 fiscal year and operating income of approximately \$916,000, before depreciation and amortization of approximately \$396,000, on gross refined product sales of approximately \$17,742,000 for the 1995 fiscal year.

There can be no assurance that the Company will successfully develop any of its undeveloped mineral properties or, if developed, that they will be commercially productive. None of the Company's undeveloped mineral properties currently produces revenues, and such properties will not produce revenues from operations to the Company unless and until exploration is completed and successful development is accomplished. Meaningful progress in some of these efforts is currently hampered by the Company's lack of sufficient operating funds.

In the case of the Al Masane project, the Company must secure the financing and construction of the mining and milling facilities before revenues from that project may be realized. The Company believes that acceptable financing for the estimated cost of the Al Masane project can be arranged, although there can be no assurance that such financing could be obtained. The results of the 1996 update to the 1994 feasibility study show the estimated total capital costs of the project to be \$88.6 million. The Coal Company's lack of significant assets, combined with the Company's lack of operating funds, inhibits any future activities of the Coal Company.

See Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations, Item 12. Security Ownership of Certain Beneficial Owners and Management and Item 13. Certain Relationships and Related Transactions for further discussion of these matters.

Foreign Operations

Since a substantial portion of the Company's mineral properties and interests are located outside of the United States, its business and properties are subject to foreign laws and foreign conditions, with the attendant varying risks and advantages. Foreign exchange controls, foreign legal and political concepts, foreign government instability, international economics and other factors create risks not necessarily comparable with those involved in doing business in the United States.

Competition

If it reaches the point of engaging in commercial mineral production, the Company expects to encounter strong competition from established mining companies which in many cases will be more extensively capitalized and have more extensive facilities and more numerous personnel than does the Company.

-11-

Personnel

In order to conserve all available funds, the Company continues to keep its general and administrative personnel to a minimum. Its only officers resident in the United States are Mr. John A. Crichton, Chairman of the Board, Mr. Jonathan Cocks, Vice President, and Mr. Drew Wilson, Jr., Secretary and Treasurer. The other employees of the Company, numbering approximately 28, consist of the office personnel and field crews conducting core drilling and other exploration activities in Saudi Arabia under the supervision of Mr. Hatem El-Khalidi, President and Chief Executive Officer of the Company. South Hampton currently employs 50 persons.

-12-
[map]

-13-

Item 2. Properties.

Saudi Arabia Mining Properties

Al Masane. The Al Masane project, which consists of an area of approximately 44 square kilometers, contains extensive ancient mineral workings and smelters. From ancient inscriptions in the area, it is believed that mining activities went on sporadically from 1000 B.C. to 700 A.D. The ancients are believed to have extracted mainly gold, silver and copper. The discussion of the Al Masane project set forth under Item 1. Business is incorporated herein by reference.

Other Saudi Arabian Areas. In 1971, the government of Saudi Arabia awarded the Company exclusive mineral exploration licenses to explore and develop the Wadi Qatan area in southwestern Saudi Arabia. The Company was subsequently awarded an additional license in August of 1977 covering an area to the north of Wadi Qatan at Jebel Harr. The licenses have expired by their terms, and although the Company has received verbal assurance from Saudi Arabian government officials that the licenses will be extended as long as exploratory work is being carried out on the areas which they cover, formal extensions from the government have not been obtained.

The Company has applied for a license covering an area surrounding the Al Masane mining lease area, which is referred to as the Greater Al Masane area. Although a license has not been formally granted for the Greater Al Masane area, the Company was authorized in writing by the Saudi Arabian government to carry out exploration work on the area. Exploration work has been carried on and paid for exclusively by the Company.

When financing for the Al Masane project is completed, the Company plans to make an application for an expanded exploration license for an area of approximately 2,800 square kilometers which includes the original Greater Al Masane area plus the Wadi Qatan and Jebel Harr areas.

Reference is made to the map on page 13 of this Report for information concerning the location of the foregoing areas.

The absence of current formal exploration licenses covering the areas on which the Company has conducted, and is continuing to conduct, exploration and development work in Saudi Arabia creates uncertainty concerning the Company's rights and obligations concerning those areas. However, the Company believes that it has satisfied the government's requirements concerning the license areas and that the government should honor the Company's claims to those areas.

In the event of the establishment of commercially exploitable minerals, exploration licenses granted by the Saudi Arabian government may be converted into mining leases upon application to the Saudi Arabian Ministry of Petroleum and Mineral Resources. The Company is a party to an agreement with Petromin, the official mining and petroleum company of the Saudi Arabian government, which governs the rights of the parties if an exploration license granted to the Company is converted into a mining lease. Reference is made to the discussion concerning the agreement under Item 1. Business.

Wadi Qatan and Jebel Harr. The Wadi Qatan area is located in southwestern Saudi Arabia. Jebel Harr is north of Wadi Qatan. Both areas are approximately 30 kilometers east of the Al Masane area. These areas consist of 40 square kilometers, plus a northern extension of an additional 13 square kilometers. Geological and geophysical work by the Company and limited core drilling disclose the existence of massive sulfides containing nickel. Preliminary core drilling to shallow depths disclosed the existence of massive sulfides containing an average of 1.2% nickel. Reserves for these areas have not been classified and more drilling is needed to classify them as proven or probable. Initial metallurgical studies by consultants to the Company in 1976 indicated difficulty in concentrating

-14-

the nickel minerals. However, in 1983 the ore was examined by a metallurgical consulting company and it was demonstrated that the ore can be treated to produce ferronickel and iron which can be used to produce steel. The proposed method could be commercially viable if enough ore is proven. Further metallurgical work by another consulting company in 1985 indicated that the ore can be treated by hydrometallurgical methods. An exploration license which includes the Wadi Qatan and Jebel Harr areas will enable the Company to continue its drilling program to prove enough ore for a viable mining operation. Although the indications are encouraging there is no assurance that a viable mining operation could be established.

Greater Al Masane. An application has been made and verbally approved for an exploration license covering approximately 1,100 square kilometers around Al Masane, sometimes referred to as Greater Al Masane, which includes an ancient gold mining prospect at Jubal Guyan, about six miles east of the original Al Masane prospect and seven miles west of Wadi Qatan. The Saudi Arabian government has given the Company written authorization to conduct exploration work on the area, although the license has not been formally granted. Core samples indicate an average grade of 7 grams of gold per tonne. Additional sampling is being conducted at Jubal Guyan, and after the results of the sampling are obtained, an evaluation will be made as to future drilling locations. Geological, geochemical and geophysical work on the Greater Al Masane area has disclosed mineralization similar to that discovered at Al Masane.

Refining Operations

South Hampton owns and operates a special products refinery near Silsbee, Texas. Gulf State owns and operates three pipelines which connect the South Hampton refinery to a natural gas line, to South Hampton's truck and rail loading terminal and to a marine terminal owned by an unaffiliated third party. The properties owned by South Hampton and Gulf State are more fully described in Item 1. Business.

Nevada Mining Properties

There are 48 patented and 81 unpatented claims totaling approximately 3,600 acres in the Pioche properties. All the claims are located in the Pioche District, Lincoln County, in southeastern Nevada. There are prospects and mines on these claims which formerly produced silver, gold, lead, zinc and copper. The ore bodies are both oxidized and sulfide deposits, classified into three groups: fissure veins in quartzite, mineralized granite porphyry and replacement deposits in carbonate rocks (limestone and dolomites). In October 1997, Pioche entered into an Exploration Agreement and Option to Purchase with a large mining company which provides for annual payments to Pioche of \$50,000 for seven years until, or unless, the mining company exercises an option to purchase an 85% interest in the mining claims for \$3 million. The agreement can be terminated upon 60 days written notice by the mining Company. The mining company has agreed to expend at least \$50,000 in exploration work each year and to drill at least one hole in the first year.

There is a 300-ton-a-day processing mill on property owned by Pioche. The mill is not currently in use and a significant expenditure would be required in order to put the mill into continuous operation.

Colorado Coal Properties

The Coal Company had a net operating loss carryforward of approximately \$5.9 million at December 31, 1997 which is limited to any future net income.

Offices

The Company has a year-to-year lease on space in an office building in Jeddah, Saudi Arabia, used for office occupancy. The Company also leases a house in Jeddah which is used as a technical office and for staff housing. The Company continues to lease office space in an office building in Dallas, Texas on a month-to-month basis. It also has a base camp and accompanying facilities and equipment at its license areas in Saudi Arabia.

Item 3. Legal Proceedings.

South Hampton, together with over twenty-five other companies, was a defendant in two proceedings pending in the 60th Judicial District Court in Jefferson County, Texas and in the 136th Judicial District Court of Jefferson County, Texas, respectively, brought on July 21, 1993 and July 18, 1994, respectively, by two former employees of the Goodyear Tire & Rubber Company plant located in Beaumont, Texas, claiming illness and diseases resulting from alleged exposure to chemicals, including benzene, butadiene and/or isoprene, during their employment with Goodyear. Plaintiffs claimed that the defendant companies engaged in the business of manufacturing, selling and/or distributing these chemicals in a manner which subjects each and all of them to liability for unspecified actual and punitive damages. South Hampton entered into settlement agreements with the two plaintiffs in March 1997 and January 1998, respectively, by agreeing to pay each plaintiff the amount of \$25,000 in full and final settlement of all claims by each such plaintiff against South Hampton. A lawsuit by another former Goodyear employee was filed in a Jefferson County District Court on December 16, 1997 alleging the same injuries and seeking unspecified actual and punitive damages. South Hampton intends to vigorously defend against this lawsuit.

In 1993, while remediating a small spill area, the Texas Natural Resources Conservation Commission ("TNRCC") requested South Hampton to drill a well to check the groundwater under the spill area. Based on the results, estimated costs of \$60,000 were accrued at December 31, 1996 to cover the recovery and remediation activity expected to take place in 1997. However, no action was taken other than further study, and another \$50,000 was accrued at December 31, 1997 for a total of \$110,000. This amount is considered adequate in that various alternative and less expensive means of recovery are being developed. Approximately \$85,000 has been expended over a three-year period to develop recovery alternatives. The consulting engineers expect approximately 10,000 barrels of recoverable material may be available to South Hampton for use in their refining process, but no reduction has been made in the accrual for estimated remediation costs due to the uncertainties relating to the recovery process. There can be no assurances that any such recovery can be made.

In November 1996, South Hampton agreed to a proposed settlement with the TNRCC's Air Permit Section for various alleged violations identified during the 1991 through 1994 inspections. An agreed fine of \$50,000 in the aggregate was paid in 1997 and 1996. South Hampton vigorously denied many of the allegations in the settlement document, but determined that further protest of the TNRCC's interpretation and application of the rules would result in higher expenses.

On August 18, 1997, the Executive Director of the TNRCC filed a preliminary report and petition with the TNRCC recommending that the TNRCC enter an enforcement order assessing administrative penalties against and requiring certain actions of South Hampton. The TNRCC alleges that South Hampton has violated various TNRCC rules, TNRCC permits issued to South Hampton, a TNRCC order issued to South Hampton, the Texas Water Code, the Texas Clean Air Act and the Texas Solid Waste Disposal Act. The violations generally relate to the management of volatile organic compounds in a manner that allegedly violates the TNRCC's air quality rules and the storage, processing and disposal of hazardous waste in a manner that allegedly violates the TNRCC's industrial and hazardous waste rules. The Executive Director of the TNRCC recommends that the TNRCC enter an order assessing administrative penalties against South Hampton in the amount of \$709,408, and recommends that the TNRCC order South Hampton to undertake such actions as are necessary to bring its operations at its refinery and its bulk terminal into compliance with Texas Water Code, the Texas Health and Safety Code, TNRCC rules, permits and orders. South Hampton intends to vigorously defend against this proceeding. A preliminary hearing was held in November 1997, but no further action has been taken to date.

On May 15, 1991, the Company filed a complaint with the U.S. Department of Justice ("DOJ") against Hunt Oil Company of Dallas, Texas ("Hunt"), alleging violations of the Foreign Corrupt Practices Act ("FCPA") by Hunt in obtaining its Petroleum Production Sharing Agreement ("PSA") in Yemen in 1981, subsequent to the Company presenting a bid to the Yemen government for the same area before Hunt made its application. The Company's Washington, D.C. attorneys opined that, because the PSA of Hunt is still ongoing, and under its auspices, payments and receipts occur daily, the DOJ still has jurisdiction to continue its investigation. A letter from the DOJ on December 19, 1995 stated its interest in receiving additional documentation regarding the Company's allegations.

On February 28, 1996, the Company sent more documents to the DOJ which it believed further supported its allegations. The Company's Washington, D.C. attorneys opined also that the Victim Restitution Act provides for restitution to the Company of monies lost as a result of the alleged wrongdoing by Hunt, if

Hunt is convicted under the FCPA. A letter from the DOJ dated October 1, 1996 stated that the documents presented did not suggest any criminal events occurred within the statute of limitations, and that, at that time, the DOJ did not intend to pursue the investigation. On November 18, 1996, legal counsel retained by the Company, after studying the facts of the case, sent the DOJ an analysis concluding that while the statute of limitations of FCPA may have lapsed, the statute of limitations for conspiracy to violate the FCPA had not lapsed, and that, as a consequence, the DOJ could criminally prosecute Yemen Hunt for conspiracy to violate the FCPA. The Company's legal counsel met with the Fraud Section of the DOJ on December 13, 1996 and were told that the DOJ would take a more aggressive stance if more information of evidentiary quality were presented to the DOJ. The Company intends to vigorously pursue obtaining such further information in the United States and in Yemen.

Late in 1994, articles were published in two prominent Yemen newspapers in which Yemen Hunt Oil Company, a wholly owned subsidiary of Hunt Oil Company of Dallas, Texas ("Yemen Hunt"), was accused of obtaining a petroleum production sharing agreement in Yemen in 1981 through the corruption of Yemen officials in order to exclude the application of the Company and its then partner, Dorchester Gas Company, from consideration for the same area. A letter to the editor of one of these newspapers, published on December 7, 1994 and signed by the executive vice president of Yemen Hunt, after explicitly mentioning the Company and Dorchester Gas Company, stated that "[Yemen Hunt] knows well those suspicious companies who are mainly engaged in political activities for the purpose of undermining the economic interest of Yemen..." On December 26, 1995, the Company filed a complaint of criminal libel with the Yemen Attorney General for Publications in Sana'a, Yemen against Yemen Hunt, alleging that Yemen Hunt, in its published letter to the prominent Yemen newspaper, had criminally libeled the Company, which, if not addressed, could seriously affect the business and reputation of the Company and its employees in the Middle East. In October 1996, the Company received the official decision from the Deputy Attorney General for Publications of Yemen which stated that, after taking the statement of the President of the Company and the statement of the chief of the legal department of Yemen Hunt, it was evident that the letter from Yemen Hunt published in the Yemen newspaper on December 7, 1994 was libelous to the Company. However, since the four month statute of limitations period under Yemen criminal law had run, Yemen Hunt could not be prosecuted for criminal libel. The Company intends to vigorously pursue the matter under the civil libel laws of Yemen.

Item 4. Submission of Matters to a Vote of Security Holders.

No matter was submitted to a vote of the Company' stockholders during the fourth quarter of 1997.

PART II

Item 5. Market for Registrant's Common Equity and Related Stockholder Matters.

This information is set forth under the caption "Market for the Company's Common Stock and Related Stockholder Matters" of the Company's 1997 Annual Report to Stockholders filed herein as Exhibit 13, which portion of such Annual Report is incorporated herein by reference.

Item 6. Selected Financial Data.

This information is set forth under the caption "Selected Financial Data" for each of the five years in the period ended December 31, 1997, of the Company's 1997 Annual Report to Stockholders filed herein as Exhibit 13, which portion of such Annual Report is incorporated herein by reference.

-17-

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.

This information is set forth under the caption "Management's Discussion and Analysis of Financial Condition and Results of Operations" of the Company's 1997 Annual Report to Stockholders filed herein as Exhibit 13, which portion of such Annual Report is incorporated herein by reference.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk.

This information is set forth under the caption "Other Matters-Quantitative and Qualitative Disclosures About Market Risks" of the Company's Annual Report to Stockholders filed herein as Exhibit 13, which portion of such Annual Report is incorporated herein by reference.

Item 8. Financial Statements and Supplementary Data.

The financial statements of the Company including the independent auditor's report thereon of the Company's 1997 Annual Report to Stockholders filed herein as Exhibit 13, are incorporated herein by reference.

Item 9. Disagreements on Accounting and Financial Disclosure.

On May 6, 1996, Price Waterhouse LLP resigned as the independent accountants of the Company. The resignation of Price Waterhouse LLP was previously reported in a Current Report on Form 8-K dated May 6, 1996.

PART III

Item 10. Directors and Executive Officers of the Registrant.

This information is set forth under the captions "Nominees for Election as Directors", "Executive Officers" and "Section 16(a) Beneficial Ownership Reporting Compliance" of the Company's Proxy Statement for the Company's Annual Meeting of Stockholders.

Item 11. Executive Compensation.

This information is set forth under the caption "Executive Compensation" of the Company's Proxy Statement for the Company's Annual Meeting of Stockholders.

Item 12. Security Ownership of Certain Beneficial Owners and Management.

This information is set forth under the caption "Outstanding Capital Stock" of the Company's Proxy Statement for the Company's Annual Meeting of Stockholders.

Item 13. Certain Relationships and Related Transactions.

This information is set forth under the caption "Other Matters" of the Company's Proxy Statement for the Company's Annual Meeting of Stockholders.

-18- PART IV

Item 14. Exhibits, Financial Statement Schedules, and Reports on Form 8-K.

- (a) 1. The following financial statements are incorporated by reference from the Company's 1997 Annual Report to Stockholders filed herein as Exhibit 13:
- Reports of Independent Accountants.
Consolidated Balance Sheets dated December 31, 1997 and 1996.
Consolidated Statement of Operations for the three years ended December 31, 1997.
Consolidated Statement of Stockholders' Equity for the three years ended December 31, 1997.
Consolidated Statement of Cash Flows for the three years ended December 31, 1997.
Notes to Consolidated Financial Statements.
2. The following financial statement schedules are filed with this Report:
- Schedule II - Valuation and Qualifying Accounts for the three years ended December 31, 1997.
3. The following documents are filed or incorporated by reference as exhibits to this Report:
- 3(a) Certificate of Incorporation of the Company as amended through the Certificate of Amendment filed with the Delaware Secretary of State on January 29, 1993 (incorporated by reference to Exhibit 3(a) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
- 3(b) Bylaws of the Company, as amended through July 6, 1994 (incorporated by reference to Exhibit 3(b) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
- 10(a) Contract dated July 29, 1971 between the Company, National Mining Company and Petromin (incorporated by reference to Exhibit 10(a) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
- 10(b) Loan Agreement dated January 24, 1979 between the Company, National Mining Company and the Government of Saudi Arabia (incorporated by reference to Exhibit 10(b) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).

10(c) Mining Lease Agreement effective May 22, 1993 by and between the Ministry of Petroleum and Mineral Resources and the Company, together with English translation thereof (incorporated by reference to Exhibit 10(d) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).

-19-

- 10(d) Stock Option Plan of the Company, as amended (incorporated by reference to Exhibit 10(e) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
- 10(e) 1987 Non-Employee Director Stock Plan (incorporated by reference to Exhibit 10(f) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
- 10(f) Phantom Stock Plan of Texas Oil & Chemical Co. II, Inc. (incorporated by reference to Exhibit 10(g) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
- 10(g) Agreement dated March 10, 1988 between Chevron Research Company and South Hampton Refining Company, together with related form of proposed Contract of Sale by and between Chevron Chemical Company and South Hampton Refining Company (incorporated by reference to Exhibit 10(o) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
- 10(h) Addendum to the Agreement Relating to AROMAX(R) Process -- Second Commercial Demonstration dated June 13, 1989 by and between Chevron Research Company and South Hampton Refining Company (incorporated by reference to Exhibit 10(p) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
- 10(i) Vehicle Lease Service Agreement dated September 28, 1989 by and between Silsbee Trading and Transportation Corp. and South Hampton Refining Company (incorporated by reference to Exhibit 10(q) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
- 10(j) Letter Agreement dated May 3, 1991 between Sheikh Kamal Adham and the Company (incorporated by reference to Exhibit 10(t) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
- 10(k) Promissory Note dated February 17, 1994 from Hatem El-Khalidi to the Company (incorporated by reference to Exhibit 10(u) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
- 10(l) Letter Agreement dated August 15, 1995 between Hatem El-Khalidi and the Company (incorporated by reference to Exhibit 10(v) to the Company's Annual Report on Form 10-K for the year ended December 31, 1995 (File No. 0-6247)).
- 10(m) Letter Agreement dated August 24, 1995 between Sheikh Kamal Adham and the Company. (incorporated by reference to Exhibit 10(w) to the Company's Annual Report on Form 10-K for the year ended December 31, 1995 (File No. 0-6247)).
- 10(n) Letter Agreement dated October 23, 1995 between Sheikh Fahad Al-Athel and the Company (incorporated by reference to Exhibit 10(x) to the Company's Annual Report on Form 10-K for the year ended December 31, 1995 (File No. 0-6247)).
- 10(o) Amended and Restated Credit Agreement dated October 15, 1996 between South Hampton Refining Company and Den norske Bank ASA, together with related Promissory Note, Ratification of Security Agreement, Ratification of Pledge Agreement, Ratification of Assignment of Insurance, Subordination Agreement,

Termination Agreement, Ratification of Subordination Agreement, Renewal, Extension and Modification Agreement, Second Lien Promissory Note and Third Lien Promissory Note of even date therewith (incorporated by reference to Exhibit 10(aa) to the Company's Annual Report on Form 10-K for the year ended December 31, 1996 (File No. 0-6247)).

- 10(p) Letter Agreement dated November 30, 1996 between Sheikh Fahad Al-Athel and the Company (incorporated by reference to Exhibit 10(bb) to the Company's Annual Report on Form 10-K for the year ended December 31, 1996 (File No. 0-6247)).
- 10(q) Financial and Legal Services and Advice Agreement dated May 20, 1996 by and among Nasir Ali Kadasah, Dar Al Khaleej and the Company, as amended by Letter Agreement dated March 3, 1997 (incorporated by reference to Exhibit 10(cc) to the Company's Annual Report on Form 10-K for the year ended December 31, 1996 (File No. 0-6247)).
- 10(r) Joint Venture Agreement dated November 5, 1997 initialed by Al Mashreq Company for Mining Investments and the Company.
- 10(s) Exploration Agreement and Option to Purchase dated as of October 21, 1997 between Homestake Mining Company of California and Pioche-Ely Valley Mines, Inc.
- 10(t) Amendment No. 1 to Amended and Restated Credit Agreement dated as of December 31, 1997 between South Hampton Refining Company and Den norske Bank ASA.
- 13 1997 Annual Report to Stockholders.

With the exception of the information incorporated by reference into Items 5, 6, 7, 7A, 8 and 14 of this Form 10-K, the 1997 Annual Report to Stockholders is not to be deemed filed as part of this Report.
- 21 Subsidiaries (incorporated by reference to Exhibit 21 to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
- 27 Financial Data Schedule.

(b) The following report on Form 8-K was filed during the last quarter of the period covered by this Report:

Current Report on Form 8-K dated October 30, 1997.

POWER OF ATTORNEY

KNOW ALL MEN BY THESE PRESENTS that each of Arabian Shield Development Company, a Delaware corporation, and the undersigned directors and officers of Arabian Shield Development Company, hereby constitutes and appoints John A. Crichton its or his true and lawful attorney-in-fact and agent, for it or him and in its or his name, place and stead, in any and all capacities, with full power to act alone, to sign any and all amendments to this Report, and to file each such amendment to the Report, with all exhibits thereto, and any and all other documents in connection therewith, with the Securities and Exchange Commission, hereby granting unto said attorney-in-fact and agent full power and authority to do and perform any and all acts and things requisite and necessary to be done in and about the premises as fully to all intents and purposes as it or he might or could do in person, hereby ratifying and confirming all that said attorney-in-fact and agent may lawfully do or cause to be done by virtue hereof.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Company has duly caused this Report to be signed on its behalf by the undersigned, thereunto duly authorized.

ARABIAN SHIELD DEVELOPMENT COMPANY

By: /s/ HATEM EL-KHALIDI

Hatem El-Khalidi, President
and Chief Executive Officer

Dated: March 30, 1998

-22-

Pursuant to the requirements of the Securities Exchange Act of 1934, this Report has been signed below by the following persons on behalf of the Company in the capacities indicated on March 30, 1998.

Signature -----	Title -----
/s/ HATEM EL-KHALIDI ----- Hatem El-Khalidi	President, Chief Executive Officer and Director (principal executive officer)
/s/ DREW WILSON, JR. ----- Drew Wilson, Jr.	Secretary and Treasurer (principal financial and accounting officer)
/s/ JOHN A. CRICHTON ----- John A. Crichton	Chairman of the Board and Director
/s/ MOHAMMED O. AL-OMAIR ----- Mohammed O. Al-Omair	Director
/s/ GHAZI SULTAN ----- Ghazi Sultan	Director

-23-

EXHIBIT INDEX

PAGE

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|-------|---|--|
| 3(a) | Certificate of Incorporation of the Company as amended through the Certificate of Amendment filed with the Delaware Secretary of State on January 29, 1993 (incorporated by reference to Exhibit 3(a) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)). | |
| 3(b) | Bylaws of the Company, as amended through July 6, 1994 (incorporated by reference to Exhibit 3(b) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)). | |
| 10(a) | Contract dated July 29, 1971 between the Company, National Mining Company and Petromin (incorporated by reference to Exhibit 10(a) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)). | |
| 10(b) | Loan Agreement dated January 24, 1979 between the Company, National Mining Company and the Government of Saudi Arabia (incorporated by reference to Exhibit 10(b) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)). | |
| 10(c) | Mining Lease Agreement effective May 22, 1993 by | |

and between the Ministry of Petroleum and Mineral Resources and the Company, together with English translation thereof (incorporated by reference to Exhibit 10(d) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).

- 10(d) Stock Option Plan of the Company, as amended (incorporated by reference to Exhibit 10(e) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
- 10(e) 1987 Non-Employee Director Stock Plan (incorporated by reference to Exhibit 10(f) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
- 10(f) Phantom Stock Plan of Texas Oil & Chemical Co. II, Inc. (incorporated by reference to Exhibit 10(g) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).

PAGE

- 10(g) Agreement dated March 10, 1988 between Chevron Research Company and South Hampton Refining Company, together with related form of proposed Contract of Sale by and between Chevron Chemical Company and South Hampton Refining Company (incorporated by reference to Exhibit 10(o) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
- 10(h) Addendum to the Agreement Relating to AROMAX(R) Process -- Second Commercial Demonstration dated June 13, 1989 by and between Chevron Research Company and South Hampton Refining Company (incorporated by reference to Exhibit 10(p) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
- 10(i) Vehicle Lease Service Agreement dated September 28, 1989 by and between Silsbee Trading and Transportation Corp. and South Hampton Refining Company (incorporated by reference to Exhibit 10(q) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
- 10(j) Letter Agreement dated May 3, 1991 between Sheikh Kamal Adham and the Company (incorporated by reference to Exhibit 10(t) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
- 10(k) Promissory Note dated February 17, 1994 from Hatem El-Khalidi to the Company (incorporated by reference to Exhibit 10(u) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
- 10(l) Letter Agreement dated August 15, 1995 between Hatem El-Khalidi and the Company (incorporated by reference to Exhibit 10(v) to the Company's Annual Report on Form 10-K for the year ended December 31, 1995 (File No. 0-6247)).
- 10(m) Letter Agreement dated August 24, 1995 between Sheikh Kamal Adham and the Company. (incorporated by reference to Exhibit 10(w) to the Company's Annual Report on Form 10-K for the year ended December 31, 1995 (File No. 0-6247)).
- 10(n) Letter Agreement dated October 23, 1995 between Sheikh Fahad Al-Athel and the Company (incorporated by reference to Exhibit 10(x) to the Company's Annual Report on Form 10-K for the year ended December 31, 1995 (File No. 0-6247)).

- 10(o) Amended and Restated Credit Agreement dated October 15, 1996 between South Hampton Refining Company and Den norske Bank ASA, together with related Promissory Note, Ratification of Security Agreement, Ratification of Pledge Agreement, Ratification of Assignment of Insurance, Subordination Agreement, Termination Agreement, Ratification of Subordination Agreement, Renewal, Extension and Modification Agreement, Second Lien Promissory Note and Third Lien Promissory Note of even date therewith (incorporated by reference to Exhibit 10(aa) to the Company's Annual Report on Form 10-K for the year ended December 31, 1996 (File No. 0-6247)).
- 10(p) Letter Agreement dated November 30, 1996 between Sheikh Fahad Al-Athel and the Company (incorporated by reference to Exhibit 10(bb) to the Company's Annual Report on Form 10-K for the year ended December 31, 1996 (File No. 0-6247)).
- 10(q) Financial and Legal Services and Advice Agreement dated May 20, 1996 by and among Nasir Ali Kadasah, Dar Al Khaleej and the Company, as amended by Letter Agreement dated March 3, 1997 (incorporated by reference to Exhibit 10(cc) to the Company's Annual Report on Form 10-K for the year ended December 31, 1996 (File No. 0-6247)).
- 10(r) Joint Venture Agreement dated November 5, 1997 initialed by Al Mashreq Company for Mining Investments and the Company.
- 10(s) Exploration Agreement and Option to Purchase dated as of October 21, 1997 between Homestake Mining Company of California and Pioche-Ely Valley Mines, Inc.
- 10(t) Amendment No. 1 to Amended and Restated Credit Agreement dated as of December 31, 1997 between South Hampton Refining Company and Den norske Bank ASA.
- 13 1997 Annual Report to Stockholders.
- With the exception of the information incorporated by reference into Items 5, 6, 7, 7A, 8 and 14 of this Form 10-K, the 1997 Annual Report to Stockholders is not to be deemed filed as part of this Report.
- 21 Subsidiaries (incorporated by reference to Exhibit 21 to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
- 27 Financial Data Schedule.

JOINT VENTURE AGREEMENT

This Agreement is made on the 5th day of November, 1997, by and between:

1. ARABIAN SHIELD DEVELOPMENT COMPANY (ASDC), a USA public stock company (Delaware corporation), with corporate offices in Dallas, Texas, USA, and a Saudi Arabian branch in Jeddah, Saudi Arabia, with Commercial Registration number 4030097805, represented in this Agreement by its president and CEO, Hatem Hussein El-Khalidi, hereinafter referred to as the "FIRST PARTY".
2. AL MASHREQ COMPANY FOR MINING INVESTMENTS (AL MASHREQ), a Saudi Limited Liability Company, with corporate office in Riyadh, Saudi Arabia, and Commercial Registration number 1010146690, represented in this Agreement by Mr. Nassir Ali Kadasah, hereinafter referred to as "SECOND PARTY".

Whereas, the First Party was awarded a Mining Lease in (Al Masane area) of 44 square kilometers area, located in the southwestern part of Saudi Arabia, by Royal Decree no. M/17, dated 1/12/1413, for the initial period of 30 years, as spelled out in the Mining Lease Agreement, attached to the said Royal Decree, and,

Whereas the First Party has conducted extensive surveys, studies, laboratory works and analysis to verify the viability of the project, and,

Whereas, the Second Party agrees to purchase from the First Party (50%) Fifty percent of First Party's beneficial interest in the project valued as indicated in Article (2) below,

And whereas the First Party desires to participate with the Second Party in the investment of this Lease by entering into a joint venture and forming a Saudi limited liability company which shall construct and operate the Mining facilities upon formation and obtaining the Industrial License from The Saudi Ministry of Industry and Electricity, and transferring the Lease to its name for the purpose of processing the ore mined in the area covered by the Lease,

THEREFORE, the Parties agree as follows:

Page 1 of 22

ARTICLE 1. DEFINITIONS

The following terms shall have the following meanings for purposes of this Agreement:

- 1.1 "AFFILIATE" means any legal person who directly controls, or is directly or indirectly controlled by, or is under common control with a Party to this Agreement. Control means ownership of and the right to vote at least eighty (80%) percent of the voting stock of the legal person and the power presently to designate a majority of the Board of Managers or equivalent body of the legal person.
- 1.2 "AGREEMENT" means this Joint Venture Agreement.
- 1.3 "ARTICLES OF ASSOCIATION" means the Articles of Association of the Arabian Shield company for Mining Industries Ltd. attached as Exhibit A.
- 1.4 "COMPANY" means the limited liability company to be established pursuant to the agreement of the Parties to implement the Project under the name "The Arabian Shield Company for Mining Industries Ltd."
- 1.5 "COMPANY'S CONFIDENTIAL INFORMATION'S" means information that the Company and Partners consider confidential, which includes but is not limited to, all technical and other information relating to the Mining Project, or generally to the manufacture of products and all economic, customer, marketing, cost, pricing, financial and other information. All of the information described in this definition constitutes

Confidential Information, whether it exists on the date of this Agreement or is developed after the date of this Agreement and whether or not the Company specifically identifies it as confidential. However, confidential Information does not include information already known to the public or those revealed or which have to be revealed by due process of law.

- 1.6 "CONSTRUCTION SCHEDULE" means the schedule for construction of the Mine(s) and its facilities.
- 1.7 "EFFECTIVE DATE" means the date on which this Agreement is executed by the Parties and approved by the Board of directors of both (ASDC) and (AL MASHREQ).
- 1.8 "FINANCIAL STATEMENTS" means the written record of the financial status of the Company, including a Balance Sheet, an Income Statement, a Statement of Cash Flow, and any

Page 2 of 22

other statements that are required or customary in Saudi Arabia.

- 1.9 "MATERIALS" means all written, drawn or otherwise recorded representations of Confidential Information, whether recorded on paper, in computer memory or other electronic devices, on magnetic tape or disks, on optical disks or on other recording media (including, for example, but not limited to, specifications, drawings, layouts and bills or materials) and any and all copies thereof.
- 1.10 "PARTNERS" means the parties hereto, and any person(s) or entity(s) who acquire Shares in the capital of the Company subsequent to the Effective Date.
- 1.11 "PROJECT" means the construction and operation of the Mine(s) and its facilities to be executed by the Company in Al Masane area as defined in the Mining Lease Agreement attached thereto.
- 1.12 "PROJECT BUDGET" means the estimate of revenue and expenditure of the Company for the period covered by the Construction Schedule.
- 1.13 "SHARES" means the capital shares of the Company having the characteristics and capitalization described in Article 5 hereof.
- 1.14 "TOTAL INVESTMENT COST" means the total amount of capital required to form the Company, to build the Mine(s) and its facilities (including without limitation fees to be paid to Contractors, sub-contractors, suppliers or equipments and materials) and to commence operation of the Mine and the Processing Plant, including the initial working capital.

ARTICLE 2. TRANSFER OF (ASDC) INTEREST

- 2.1 "AL MASHREQ" acknowledges that (ASDC) has acquired the beneficial interest in the project by obtaining the Mining Lease in its name and by incurring a substantial expenses in connection therewith.
- 2.2 The Parties agreed to value that interest at (26) twenty six million US Dollars.
- 2.3 (ASDC) offers to sell and (AL MASHREQ) accepts to purchase 50% (fifty percent) of that interest at a lump-sum price of (13) thirteen million US Dollars.

Page 3 of 22

- 2.4 (AL MASHREQ) agrees to pay to (ASDC) the sum noted in Par 2.3 above promptly, in full, at the time the title to the Mining Lease is transferred to the new Company "The Arabian Shield Company for Mining Industries".

ARTICLE 3. ORGANIZATION OF THE COMPANY

3.1 LICENSE AND FINANCING

- (a) The two Partners shall, commencing immediately as of the Effective Date, work in good faith together to apply for and to obtain a foreign capital investment license for the Company pursuant to the Foreign Capital Investment Code of Saudi Arabia, to establish the Company for the purposes set forth in Article (4) of this Agreement and to transfer the Mining Lease into the name of the Company.
- (b) The Partner shall, commencing immediately as of the Effective Date, work in good faith together to apply for and obtain the maximum financing available on the most favorable possible terms from the Saudi Industrial Development Fund and local commercial or other financing as necessary so that the sum of the total amount of debt and the stated capital of the Company equals or exceeds the Total Investment Cost. If they fail, within twelve months after the Effective Date, to obtain firm commitments for financing the project on an acceptable terms, then they shall be entitled to terminate this Agreement upon notice to the other Partners, without any liability or obligation whatsoever to the Company, any Partner or any prospective Partner, except for amounts paid to (ASDC) by (AL MASHREQ) in consideration of the beneficial interest being assigned by (ASDC) to (AL MASHREQ), if any, which amounts shall be promptly recovered by (AL MASHREQ) upon liquidation of the Company or under any other possible arrangements between the Parties. In this case, the full title to the Mining Lease shall revert to (ASDC).
- (c) The (ASDC) shall perform or cause one of its affiliates to perform an economic feasibility study as reasonably required to support the efforts to obtain the financing required for the Company. Such study shall be in accordance with S.I.D.F. requirements.

Page 4 of 22

- (d) The Company will, after its formation, use its knowledge of the Saudi legal and commercial system and its best efforts to facilitate the financing referred to above. Both before and after the formation of the Company, (Al Mashreq) shall exert its best efforts to assist the Company to facilitate the licensing and financing referred to above and to assist the Company with the Project.

3.2 REGISTRATION OF THE COMPANY

The Partners shall begin immediately to prepare all required procedures for the formation and registration of the Company as a limited liability company in accordance with Part VII of the Companies Law promulgated by Royal Decree No. M/6 of 22.3.1385 H. (as amended) (the "Companies Law"). The Company shall have the characteristics set out in the Articles of Association attached as Exhibit A and incorporated herein by reference. The Arabic text of these Articles of Association shall be used for registration purposes in Saudi Arabia. To the extent that the terms of this Agreement are not incorporated into the Articles of Association, the unincorporated terms shall be deemed the by-laws of the Company.

3.3 CERTAIN OTHER APPLICATIONS

The Partners shall exert their best efforts to establish the Company so as to qualify for the various incentives available under the Foreign Capital Investments Law of Saudi Arabia and for other benefits and protections available under the rules and regulations of Saudi Arabia.

3.4 PREVALENCE OF THIS AGREEMENT

The Articles of Association are intended by the Partners to be fully consistent with this Agreement. If there is any discrepancy between

the provisions of this Agreement and the Articles of Association, this Agreement shall govern as between the Partners. All Partners shall exercise their voting rights at each of the general meetings of the Partners, and they shall cause their representatives and nominees on the Board of Managers of the Company, to do and perform all acts, deeds and things as may be necessary or expedient to give effect to the terms and intent of this Agreement.

Page 5 of 22

ARTICLE 4. OBJECTIVES AND PURPOSES

The main objectives and purposes of the Company shall be:

- 1) Yearly production of 35,000 tonnes of Copper Concentrate.
- 2) Yearly production of 59,000 tonnes of Zinc concentrate.
- 3) Yearly production of 7.650 ounces of Gold in Dore.
- 4) Yearly production of 375,000 ounces of Silver in Dore.

These amounts shall be processed from the Ore mined from AL MASANE mines at the initial rate of (700,000) Seven Hundred Thousands tonnes per annum.

ARTICLE 5. CAPITALIZATION

5.1 STATED CAPITAL

The Company shall have a stated capital of Ninety Seven Million Five Hundred Thousand Saudi Riyals (SR 97, 500,000 divided into Nine Thousands Seven Hundred and Fifty (9,750) indivisible shares valued at Ten Thousand Saudi Riyals (SR 10,000) each. Each Partner shall pay, in full, the amount of its portion of capital as provided in Section 5.4.

5.2 EQUITY PERCENTAGES

Each of the two Partners shall own 50% of the shares of the Company.

5.3 SHARE REGISTER

In accordance with Article (166) of Part VII of the Saudi Companies Act, the Company shall prepare and maintain a special register in which shall be entered the names of the Partners, the number of shares owned by each and any transfers of shares permitted by this Agreement.

5.4 CAPITAL ACCOUNT

The Company-under-formation shall establish at a bank in Saudi Arabia a capital account which shall be funded on a timely basis with each Partner's capital contribution, to be deposited in such bank which will issue a certificate evidencing such deposit. No Partner shall receive interest on such contribution, which shall be made in cash at the latest time permitted by the Ministry of Commerce or other appropriate authority. The funds shall be available to the

Page 6 of 22

Company upon satisfaction of the Company's obligations as set out in Article 162 of the Companies Act.

5.5 PERCENTAGE INTEREST IN PROFITS AND LOSSES

The Partners shall share the profits and losses of the Company in proportion to their respective shares of equity ownership. The profits of the Company, if any, available for distribution after making provision for the statutory reserve or for other reserves established by the unanimous vote of Partners, shall, to the extent permitted by the terms of the Company's financing, be distributed annually in full to the Partners in accordance with the relevant provisions in the Saudi Company Law. The losses shall be borne by the Partners up to the maximum of their

respective interests in the Share Capital of the Company.

5.6 COMPUTATION OF PROFITS

For the purpose of this Agreement, profits or losses shall mean gross receipts from any and all operations carried out by the company less all expenses, direct and indirect, properly attributable thereto, as determined by the audited financial statements of the Company.

5.7 TAXATION

The Company shall withhold from each Partner and shall pay directly to the Saudi Arabian government any and all applicable Saudi Arabian income taxes, Zakat or social insurance levies which are due and payable. Each Partner shall be responsible for all applicable income taxes, Zakat and other liabilities relating to their respective portion of the Company's distributed profits.

ARTICLE 6. TRANSFER OR DISPOSITION OF SHARES

- (a) Subject to the provisions of the Company's Articles of Associations, each of the Partners may transfer Shares to the other or to a designee of the other that is permitted to own the transferred shares under Saudi Law.
- (b) (ASDC) and (Al Mashreq) may transfer Shares to any of their Affiliates if the transferee agrees in writing to be bound by this Agreement and any other obligations previously accepted by the transferor.

Page 7 of 22

- (c) The parties agree and acknowledge that each Partner of the Company has been selected on the basis of its unique contribution to the Company and its activities. The parties also agree that it is highly desirable that this ownership group be maintained and that in the event that a Partner must dispose of its interest in the Company that the other Partner be able to participate in the selection of those entities that will acquire the departing Partner's interest. Therefore, in any such event, the departing Partner will cooperate to the maximum extent possible with the remaining Partner to facilitate these objectives. For instance, if a Partner is about to be liquidated or declared bankrupt or is required by a court order to transfer any of its Shares, then that Partner shall offer to the remaining Partner the right to purchase its shares at a mutually agreed price.

ARTICLE 7. MEETING AND VOTING OF PARTNERS

7.1 ANNUAL GENERAL MEETINGS:

Partners Annual General Meetings, shall be conducted as provided in the Articles of Association. The general meeting shall be at the Company's principal office unless the Partners agree otherwise.

7.2 SPECIAL MEETINGS

Extraordinary general meetings shall be convened at any time, with at least twenty-one (21) days written notice, upon the request of any Partner, the request of (3) Board Managers or the request of the Company's auditor. Such request shall clearly specify the matters to be discussed.

7.3 VALIDITY OF PARTNER ACTION

Annual general meetings and extraordinary general meetings of the Partners shall be valid if all Partners are present or duly represented, and that they have been given the (21) days notice required under the Articles of Association. No resolution or other action of the Partners shall be considered adopted or approved unless it has received the affirmative votes of all Partners.

7.4 ACTS THAT REQUIRE PARTNERS ACTION

The following actions of the Company may not be taken unless approved by a resolution of a General Meeting of Partners:

- (a) Appointment and removal of the Company's auditors;
- (b) Approval of the Financial Statements of the Company;
- (c) Amending the Articles of Association of the Company;
- (d) Changing the Stated Capital of the Company;
- (e) Amalgamating the Company's business with that of another company;
- (f) Dissolving or terminating the Company except as provided in this Agreement;
- (g) Changing the principal business or objectives of the Company;
- (h) The disposition or encumbrance of all or substantially all of the assets of the Company (by a single transaction or a series or transactions) whether by sale, lease, mortgage or pledge;
- (i) Any change in the scope of or nature of powers and authorities vested in the Board of Managers and Executive General Manager.
- (j) Approval of distribution of dividends; and
- (k) Any other matters reserved to the exclusive jurisdiction of a General Meeting under the law of Saudi Arabia.

ARTICLE 8. BOARD OF MANAGERS

8.1 BOARD OF MANAGERS

The Board of Managers of the Company shall be composed of Six persons.

8.2 APPOINTMENT OF MANAGERS

Upon issuance of the Company's Commercial Registration Certificate, the Partners shall appoint the Managers comprising the Board of Managers as set forth below. Each of the two Partners shall appoint three Managers from its side and shall be entitled to dismiss and replace at will any of such managers nominated from its side by giving written notice thereof to the other Partners. If a Manager

resigns, dies or if removed from office, the Partner that originally appointed such Manager shall appoint his successor. The Chairman of the Board of Managers shall be appointed by the Board from the Managers designated by (Al Mashreq) and he shall not have a casting vote.

In its First meeting, the Board shall also appoint, by a formal resolution, an "Executive Manager" from the Managers nominated by (ASDC).

8.3 MEETINGS OF BOARD OF MANAGERS

The Board of Managers shall meet from time to time, but no less often than two times per year, for the purpose of (a) determining and supervising the implementation of significant policy matters affecting the business and affairs of the Company, (b) deciding those matters set forth in Section 8.6 of this Agreement.

8.4 DUTIES OF CHAIRMAN

The Chairman shall be to preside at all meetings of the Board of Managers, unless he is absent, in which case a Manager designated by the present members shall preside. The Chairman shall also exercise, subject

to the approval of the Board when necessary, the following powers:

- i. represent the Company in the execution of contracts and agreements with governmental and non governmental institutions.
- ii. Pledge the Company's assets, fully or in part, before appropriate judicial authorities.
- iii. Opening of bank accounts and execution and issuance of bank facilities, securities and guaranties for the Company and in its name.

The Chairman may delegate any of these authorities to the Executive Manager or to any other official of the Company.

8.5 VALIDITY OF BOARD OF MANAGERS ACTION

Meetings of the Board of Managers shall be valid if and only if a quorum of at least (four) Managers is present in person or by proxy and all Managers have received a (15) days prior written notice of the meeting and of the agenda for the meeting, or consented in writing to waive the agenda requirement and/or to such shorter notice as the members may agree to. Meetings of the Board of Managers may

Page 10 of 22

be held inside or outside Saudi Arabia. If a quorum is not present, the meeting shall be reconvened upon notice to all Managers at a date not less than four (4) and no more than ten (10) days thereafter. The quorum for such reconvened meeting shall be at least four Managers. No resolution or other action of the Board of Managers shall be considered adopted unless it has received the affirmative votes of at least four managers.

8.6 ACTS THAT REQUIRE BOARD OF MANAGERS ACTION

The Executive Manager shall not cause the Company to take any of the following actions without the adoption of a resolution specifically approving such action by the Board of Managers:

- (a) Recommendation of dividends to the General Meeting;
- (b) Other than as set forth in the Project Budget, any expenditure or commitment by the Company in excess of one million Saudi Riyals (SR 1,000,000) in the aggregate in any one year or four hundred thousand Saudi Riyals (SR 400,000) for any one transaction.
- (c) Any loans by the Company to any Partner;
- (d) Authorizing the Company to take loans or leases with a term longer than five years;
- (e) Authorizing loans to Managers, employees or third parties other than advances to trade debtors or expense advances to employees in the ordinary course of business;
- (f) Selling or otherwise disposing of real property;
- (g) Selling or otherwise disposing of any assets of the Company having a value of more than one million Saudi Riyals (SR 1,000,000) in the aggregate in any one transaction, other than sales of inventory in the ordinary course of business; and
- (h) Approval of the Project Budget and Construction Schedule.

8.7 PARTICIPATION BY PROXY

Managers may attend and vote at meetings of the Board of Managers in person or by proxy given to another Manager consistent with the Articles or Association.

8.8 ACTION BY WRITTEN CONSENT

The Board of Managers shall be entitled to adopt a valid resolution without a meeting by a written resolution approved and signed by (all) of the Managers.

ARTICLE 9. MANAGEMENT

9.1 EXECUTIVE MANAGER IN OVERALL CHARGE

The day-to-day management of the Company shall be entrusted to the Executive Manager who shall report to the Board of Managers in connection with his duties.

9.2 POWERS OF MANAGEMENT

In its first meeting, the Board of Managers shall adopt a resolution specifying the authorities and responsibilities of the Executive Manager.

9.3 VIEWS ON THE PERFORMANCE OF THE CHAIRMAN AND THE EXECUTIVE MANAGER

If any of the Partners have any complaints or views with respect to the performance of the person appointed as Chairman or Executive Manager, as the case may be, such a Partner shall promptly advise the other Partner of those views or concerns. In this case both Partners shall sit together to consider and resolve such complaints or views. If no agreement is reached in that respect within (60) days period, the Board of Managers shall adopt a resolution removing the Chairman or Executive Manager whose performance or behaviour is under discussion. The relevant Partner shall then name an other person to substitute the one so removed.

9.4 SUPERVISION OF CONSTRUCTION

The Partners acknowledge and agree that, while the project is under construction, (ASDC) or one of its Affiliates will provide a project manager for the Project. The project manager shall have overall responsibility and authority for the construction and supervision of the project. The project manager shall keep the Board advised of his activities and of all significant developments with respect to the project. The Project Manager appointed per this clause is a Company's officer, and as such, the Company will be responsible for his compensation.

9.5 COMPANY TO APPOINT CERTAIN OFFICIAL

Upon recommendation from the Executive Manager, the Board shall appoint qualified persons to serve as (Financial Director), (Operations Director) and (Marketing Director) of the Company. The Finance Director, Operations Director and Marketing Director may be removed from office by a resolution of the Board of Managers as may be recommended by the Chairman of the Board or by the Executive Manager.

9.6 OTHER EMPLOYEE ACTIONS

The Executive Manager will have the responsibility and right to engage and dismiss all other employees of the Company.

9.7 GENERAL MANAGER'S AUTHORITY TO SIGN

The Parties agree that it shall require the signature of the Executive Manager to bind the Company toward third persons, except where a resolution of the Board of Managers expressly authorizes another person to sign, or when the matter falls under the authority of the Chairman as per the Company's Articles of Association. From time to time, the Board shall take such action as may be necessary to effect the grant of authority which action may include the granting of further or more specific powers of attorney.

9.8 SIGNATURE OF CHECKS

The Partners agree that all Company checks shall require co-signature, except as the Board of Managers may otherwise provide. The Board of Managers by duly made resolution shall designate persons authorized to sign checks made on behalf of the Company.

ARTICLE 10. BOOKKEEPING AND ACCOUNTING

- 10.1 FISCAL YEAR: The fiscal year of the Company shall commence as of January 1 of each year, except for the first fiscal year which, to the extent permitted by Saudi laws, will commence on the date of issuance of the Commercial Registration Certificate of the Company, and shall end on December 31 of that year or the following year, as the Company elects.
- 10.2 FINANCIAL STATEMENTS AND OTHER RECORDS: The financial books and records of the Company, including annual Financial Statements, shall conform to generally accepted

Page 13 of 22

international accounting principles a Saudi Arabia's legal requirements. Each of the Partners shall be granted the right at any reasonable time during normal business hours of the Company, to have full access to the books and records of the Company in order to review and examine same at the expense of the requesting party.

- 10.3 REPORTS TO PARTNERS: The Company shall provide to each of the Partners quarterly accounts and such periodical or incidental reports concerning the financial status of the Company as the Partners, may reasonably request.
- 10.4 ANNUAL FINANCIAL STATEMENTS: The annual Financial Statements of the Company shall be audited by a firm of registered public accountants of international standing having an office in Saudi Arabia, designated by a resolution of the Partners in accordance with the provisions of this Agreement.

ARTICLE 11. CONFIDENTIALITY AND COMPETITION

11.1 CONFIDENTIALITY:

- (a) The Company, and each Partner shall keep strictly secret and confidential any and all Confidential Information relating to the Company and/or to the project and shall not, in any manner whatsoever, disclose or permit any of its agents, representatives, employees, attorneys, accountants or advisors to disclose any Confidential Information to any person or entity whatsoever without the prior written consent of the relevant authority. The Company and each other Partner shall take all necessary steps to safeguard the secrecy and confidentiality of all Confidential Information and all Materials and to ensure that such Confidential Information and Materials obtained in connection with this Agreement are disclosed only to Authorized Persons who need to know such information for the purpose of performing their duties on behalf of the Company (or their required official government functions).
- (b) The confidentiality obligation under this section shall not apply to such a portion of the Confidential Information (if any) which is or become generally available to the public other than as a result of a disclosure by the Company, any Partner, any Affiliate, any of their respective representatives or any other

Page 14 of 22

person or entity that has an obligation not to disclose such information.

- (c) Each Partner shall be responsible and liable to the Company for any breach of this Section (11) by its Affiliates, agents, representatives, employees, attorneys, accountants or advisors.

- (d) A disclosure by Partners to any of their Affiliates or their officers, directors or employees does not constitute a violation of this Article (11).
- (e) All of the provisions of Article (11) shall continue to apply to each Partner (a) even if he or it ceases to be a Partner for any reason; or (b) if this Agreement is terminated for any reason.

11.2 COMPETITION

Each of the Partners agrees that during the term of this agreement it shall not: (I) directly, or indirectly through affiliates or through other related entities as to which it has significant influence over management decisions, enter into activities within the Company activity domain which are in competition with the Company's mining business or (ii) own or hold an ownership interest in or grant any license or provide any technical information to any entity(s) which does business in the Company's Area in competition with the Company's business.

Each of the Partners agrees that for a period of (10) years beginning as of the date on which ground is broken for the construction of the project, it shall not own, hold an ownership interest in or grant any technology license to any entity having or intending to have the same or similar business within the Company's Area.

ARTICLE 12. DURATION, TERMINATION AND DEFAULT

12.1 PERPETUAL DURATION OF THE COMPANY

The duration of the Company shall be an initial term of (50) years from the date of issuance of its Commercial Registration Certificate with automatic renewal(s) for successive terms of (15) years each unless, at least one year before the expiration of any term, a Partner(s) owning at least 50% of the Company's shares notify the other Partner(s) of its intention to cause the liquidation of the Company. The Company will continue in existence

Page 15 of 22

notwithstanding the death, cessation of existence or withdrawal of a Partner.

12.2 TERMINATION

- (a) At any time after construction of the Mining Plant(s) has commenced, this Agreement may not be terminated except by agreement of all Partners.
- (b) If, at any time before construction of the Mining Plant begins, either Partner;
 - (i) becomes bankrupt or insolvent or files a petition therefor;
 - (ii) makes an assignment for the benefit of creditors;
 - (iii) has a receiver appointed over all or substantial part of its assets;
 - (iv) commences or has commenced against it proceedings for winding up or dissolution except in connection with any reorganization, recapitalization, restructuring or amalgamation or merger; or
 - (v) commits a serious breach with respect to any significant provision of this Agreement or any other agreement entered into by it in accordance with this Agreement;

then the other "Aggrieved Party" may serve written notice of default upon the defaulting Partner. In such event, the defaulting Partner shall be allowed (30) days to cure the default. If the default is not cured on a timely basis to the satisfaction of the Aggrieved Party, then the Aggrieved Party shall be entitled to terminate this Agreement upon (30)

days written notice.

12.3 EFFECT OF TERMINATION FOR BREACH

If this Agreement is terminated as provided in Section 12.2(b) above, then: (a) the Partner whose action or breach gave rise to the right to terminate shall, subject to applicable Saudi Arabian law, sell all of its shares of the Company to the Aggrieved Party or to a person or entity designated by the Aggrieved Party; (b) the other Partner(s) other than the Partner whose default occasioned the termination shall be entitled to all damages or other remedies provided by applicable law; and (c) all of the obligations of the Partners under all other Articles of

Page 16 of 22

this Agreement and any other Agreement executed pursuant to this Agreement shall be terminated with respect to the Partner that has defaulted, except for obligations of confidentiality, which shall survive the termination of the Agreement.

12.4 EFFECT OF TERMINATION FOR FAILURE OF CONDITIONS

If this Agreement is terminated because of failure to obtain the Industrial Licence or to transfer the Lease in the name of the Company pursuant to Article 2.1(a), then any other agreement executed pursuant or related to this Agreement and each Partners' obligations under any such other agreement shall be terminated except for obligations of confidentiality which shall survive the termination of the Agreement. If this Agreement is terminated because of failure to provide sufficient financing for the project pursuant to Article 2.1(b) and the Company has received its Commercial Registration previously, then the Company shall be liquidated in accordance with the Companies Law and any other agreement executed pursuant or related to this Agreement and the Partners' obligations under any such other agreement shall be terminated except for obligations of confidentiality, which will survive the termination of the Agreement.

ARTICLE 13. GOVERNING LAW AND LANGUAGE AND SETTLEMENT OF DISPUTES

13.1 GOVERNING LAW

This Agreement shall be governed by and construed in accordance with the laws of Saudi Arabia.

13.2 LANGUAGE

This Agreement, all communications to each Partner hereunder, all information, plans, specifications, instructions and services provided hereunder, and the proceedings of the Partners shall be executed, given and conducted in the English language. An Arabic translation of this Agreement will be made available to each Partner at the expense of the Company.

13.3 ARBITRATION

The procedure for resolution of disputed under this Agreement shall be as follows:

Page 17 of 22

- (a) Any dispute or claim between the Partners arising out of or in connection with this Agreement or the breach, invalidity or termination hereof shall be settled if possible in the first instance amicably. If amicable settlement cannot be reached, the matter under dispute shall be resolved by arbitration. This arbitration clause shall be deemed to be an agreement independent of the other terms of the Agreement.
- (b) The arbitration shall be conducted in Saudi Arabia by a three-member board of arbitrators in accordance with the Arbitration Rules of the Kingdom of Saudi Arabia, pursuant to Royal Decree No. M/46 of 12.7.1403. Each party shall select one arbitrator and the two arbitrators so chosen will select the third

arbitrator, who shall be chairman of the board of arbitrators.

- (c) The decision of the board of arbitrators, which shall be determined by a majority vote, shall be final and the Partners agree and acknowledge that any award rendered by such board may be executed in any court of competent jurisdiction. In its deliberations, the board of arbitrators shall apply the provisions of this Agreement.
- (d) The official language of the arbitration shall be Arabic unless the arbitrators agree to conduct the same in English. The Partners agree that an English translation of all submissions made to the arbitration panel in Arabic will be provided to the other Party(s) by the submitting party at the submitting party's cost. Each Partner irrevocably consents to conducting any arbitration in English, if the arbitrators will agree to do so.
- (e) The award of the arbitrators will be final with respect to all controversies. Each party shall bear its own costs in the arbitration, including the fees and expenses of the arbitrator selected by it. The arbitrators shall decide which party shall pay the fees and expenses of the third arbitrator.
- (f) The award of the arbitrators shall be enforceable by any court having jurisdiction over the Party or Parties against which the award has been rendered, or where assets of the Party or Parties against which the award has been rendered can be located.

Page 18 of 22

- (g) Each of the Parties agrees to pay the amount of any arbitration award and of any costs and expenses of arbitration which the arbitrators determine that it is required to pay within sixty (60) calendar days after receipt of notice of the arbitrators' final award.

ARTICLE 14. ADDITIONAL OBLIGATIONS

14.1 RECRUITING SAUDI MANAGEMENT PERSONNEL

The Company shall make a diligent effort, to identify, recruit and train management personnel from among Saudi Arabian national who, after training, can gradually replace the expatriate technical employees of the (ASDC) who are providing services for the Company on secondment basis. The Arabian Shield Development Co. shall provide training to such individuals in the Mining business in the most advanced technical and management methods and techniques.

14.2 OTHER OBLIGATIONS OF (ASDC)

As long as the (ASDC) owns 50% of the Shares, it shall make available to the Company all technical information, developments and modernization necessary for the business improvement. Such an obligation shall extend to the U.S.A, Delaware, parent company the (Arabian Shield Development Co.), who shall provide the Company and its Saudi Arabian subsidiary (ASDC) with all technical support during the term of this Agreement in, connection with the performance of the latter's obligations under this Agreement.

ARTICLE 15. MISCELLANEOUS

15.1 NO ASSIGNMENT

No Party to this Agreement may assign, transfer or otherwise convey any or all of its rights or delegate its duties hereunder without written consent of the other Party(s), except as expressly provided in this Agreement or in the Company's Articles of Association; and any attempt to do so will be void. Permitted transfers can only be valid if the person or entity that acquires Shares in a manner allowed by this Agreement binds itself in writing, to the obligations and duties set forth in this Agreement.

Page 19 of 22

IN WITNESS WHEREOF, the Parties hereto have executed this Agreement as of the date first written above.

AL MASHREQ MINING INVESTMENTS CO.

By:

Name: Nassir Ali Kadasah

Title: Authorized Attorney

Page 21 of 22

ARABIAN SHIELD DEVELOPMENT CO. LTD.

By:

Name: Hatem Hussein Al Khaldi

Title: President

Page 22 of 22

EXPLORATION AGREEMENT
AND
OPTION TO PURCHASE

EXPLORATION AGREEMENT WITH OPTION TO PURCHASE (the "Agreement") dated as of October 21, 1997, ("Effective Date") among HOMESTAKE MINING COMPANY OF CALIFORNIA, a California corporation, having its principal place of business at 650 California Street, San Francisco, CA 94108 ("Homestake") and PIOCHE-ELY VALLEY MINES, INC., a Nevada corporation, having its principal place of business at 10830 North Central Expressway, Suite 175, Dallas, Texas 75231 ("Pioche-Ely Valley").

1. Property. The property subject to this Agreement includes those certain patented and unpatented mining claims owned by Pioche-Ely Valley all more particularly described in Exhibit A hereto, hereafter collectively referred to as the "Property".

2. Representations; Indemnity of Pioche-Ely Valley.

(a) Homestake represents to Pioche-Ely Valley and Pioche-Ely Valley represents to Homestake that (i) the representing corporation is a corporation duly incorporated and in good standing in its state of incorporation; (ii) the representing corporation is qualified to do business and is in good standing in the State of Nevada; (iii) all corporate and other actions required to authorize the representing corporation to enter into and perform this Agreement have been properly taken; (iv) the representing corporation is not and will not be after the giving of notice and passage of time, in breach or violation of any other agreement or obligation by entering into or performing this Agreement or any transaction contemplated by it; (v) this Agreement has been duly executed and delivered by the representing corporation; and, (vi) this Agreement is valid and binding upon the representing corporation in accordance with its terms.

(b) Pioche-Ely Valley represents that it is in exclusive possession of and owns a 100% undivided interest in and to the Property, subject only to the paramount title of the United States in that portion of the Property comprised of unpatented mining claims, except for that portion of the Property known as the Poorman Area more particularly described in Exhibit A - Part II, in which the Pioche-Ely Valley owns an 85% undivided interest.

(c) Pioche-Ely Valley represents that to the best of its knowledge and as of the Effective Date of this Agreement the unpatented claims included in the Property have been properly located and monumented; location and any required validation work have been properly performed; location notices and certificates have been properly recorded or filed; all filings required to maintain the unpatented mining claims in good standing, including evidence of location and assessment work, or the equivalent thereof, under the Federal Land Policy and Management Act of 1976, 43 U.S.C. Section 1744, and other applicable state, federal and local law, have been properly made; all assessment work required to hold the unpatented mining claims has been properly performed (or deferred or excused) through the assessment year ending September 1, 1992; and all required affidavits of assessment work have been properly and timely filed.

(d) Pioche-Ely Valley represents that as of the Effective Date all rentals to the United States government pursuant to the United States Interior and Related Agencies Appropriations Act of 1993 and the Omnibus Budget Reconciliation Act of 1993 required to be paid to hold the unpatented claims included in the Property in good standing through August 31, 1998 have been paid in a timely manner and affidavits of payment of maintenance fees and of intention to hold mining claims have been properly and timely recorded in Lincoln County.

(e) Pioche-Ely Valley represents that the Property is free and clear of all mortgages, liens, charges, pledges, security interests and encumbrances, including any lease, right or license, except taxes not yet due and payable. Prior to the formation of the Joint Venture contemplated by Section 11 and while this Agreement is still in effect, Pioche-Ely Valley at its own expense shall take all action necessary to cure any defect in or remove any cloud on

title to the Property suffered or allowed by such party, including participation in judicial proceedings and recordation of any unrecorded documents. If after notice or demand to take any such action, Pioche-Ely Valley fails to do so, such failure shall constitute the irrevocable authorization for Homestake to take all such action in such party's name and credit the reasonable costs and expenses of doing so, including attorney's fees, against the Purchase Price provided for in Section 5(b) or any other amounts payable to Pioche-Ely Valley hereunder or under the Joint Venture contemplated by Section 11; provided, in any event Homestake shall be solely responsible for removing any lien or encumbrance now or subsequently placed on the Property related to Homestake's work or operations on or in respect to the Property. Each party agrees to cooperate with the other party and to take such reasonable actions, execute and deliver such reasonable documents, and otherwise provide such reasonable assistance as is useful or necessary to permit the cure of any title defect.

(f) Pioche-Ely Valley makes no representation or warranty whatsoever, express or implied, as to the existence of any discovery on any of the unpatented claims constituting the Property.

(g) Pioche-Ely Valley represents to Homestake that as of the date of its execution of this Agreement and except as disclosed in that certain Property Transaction, Pioche-Ely Valley Mines, Phase I and Phase II Environmental Assessment, Preliminary Draft dated June 20, 1997 prepared by JBR Environmental Consultants, (i) Pioche-Ely Valley has no knowledge of any toxic or hazardous

-2-

substances on, in or under the Property; (ii) Pioche-Ely Valley has no notice or knowledge of any release or discharge of any toxic or hazardous substance from the Property at any time or times; and (iii) Pioche-Ely Valley has no notice or knowledge of any investigation or proceeding by any federal, state or local government or agency thereof that might lead to the listing some or all of the Property under the Comprehensive Environmental Response and Liability Act of 1980, as amended, or any state or local law or regulation dealing with the control of toxic or hazardous substances, materials or wastes. Pioche-Ely Valley agrees to defend, indemnify, and hold Homestake and its Affiliates harmless from all cost, liability, loss, damage, claim, expense or contribution, including reasonable attorneys' fees, arising out of or related to any breach of the representations contained in this Section 2, all of which shall survive termination of this Agreement, including any termination arising out of exercise of the vesting of Homestake's interest as provided in Section 11. For all purposes of this Agreement "Affiliate" shall mean any person, partnership, joint venture, corporation or other form of enterprise which directly or indirectly controls, or is controlled by, or is under common control with, a signatory. For purposes of the preceding sentence, the word "control" shall mean possession, directly or indirectly, of the power to direct or cause direction of management and policies through ownership of voting securities, contract, voting trust or otherwise.

3. Liens; Title.

(a) Pioche-Ely Valley shall not during the term of this Agreement create, suffer or allow any liens or encumbrances on the Property without the consent of Homestake or unless expressly subordinated to Homestake's rights hereunder. Except for liens or encumbrances consented to or subordinated to Homestake's interests as expressly provided above, Homestake, at its option, may discharge any lien or encumbrance on the Property or any interest therein, acquire all the rights of the holder thereof, and credit Homestake's reasonable costs and expenses of doing so, including reasonable attorney's fees, against Expenditures.

(b) Upon execution hereof, Pioche-Ely Valley shall provide Homestake with copies of all data and information in Pioche-Ely Valley's or its Affiliates' possession related to title to the Property and copies of all unrecorded documents related thereto in Pioche-Ely Valley's or its Affiliates' possession.

(c) Neither Homestake's execution of this Agreement, nor Homestake's failure to disapprove Pioche-Ely Valley's title, shall constitute an admission of or estoppel as to the validity of Pioche-Ely Valley's title to all or any part of the Property.

(d) Pioche-Ely Valley shall at its sole cost and expense, use good faith efforts to immediately acquire the outstanding 15% interest in the Poorman Area and all such interests acquired by Pioche-Ely Valley shall automatically be subject to the terms

-3-

and conditions of this Agreement and the Joint Venture Agreement contemplated by Section 11 without further payment or obligation on the part of Homestake. Pioche-Ely Valley shall give notice of its acquisition of any of the outstanding interest(s) to Homestake within 15 days following such acquisition and Homestake and Pioche-Ely Valley shall execute and deliver to Homestake an appropriate amendment to this Agreement reflecting such ownership. In the event Pioche-Ely Valley is not successful in acquiring some or all of the outstanding interests in the Poorman Area within 120 days following the Effective Date, then Homestake may acquire the outstanding interests; any such interest so acquired shall be subject to the terms and conditions of this Agreement and any amounts paid for such interests shall at Homestake's election be credited against either Homestake's expenditures pursuant to Sections 7(a) and (b) or payments pursuant to Section 8(b). If Homestake's interest vests pursuant to Section 11 at a time when neither Pioche-Ely Valley nor Homestake have acquired the Poorman Area, then Homestake shall have earned and vested its interest in 100% of the 85% undivided interest owned by Pioche-Ely Valley in the Poorman Area and Pioche-Ely Valley shall have no right, title, or interest of any kind in or to the Poorman Area.

4. Homestake's Right to Possession and Use; Conditions of Use.

During the term of this Agreement and subject to the terms and conditions of this Agreement, Homestake shall have the sole and exclusive possession, occupancy and the quiet enjoyment of the Property and the exclusive rights to carry out such geological, geochemical, and geophysical tests and investigations as are useful or necessary to determine whether Homestake desires to develop a commercial mining operation on the Property under the terms and conditions of this Agreement, including but not limited to the rights to:

(i) enter, occupy, use, explore and evaluate the Property and to extract, remove, store and dispose of in connection with such exploration and evaluation such quantity of ores, minerals, water and waste as is reasonably useful or necessary by means of underground or surface mining and sampling techniques and workings including but not limited to drilling and bulk sampling by Homestake;

(ii) use any part of the Property for stockpiles and waste dumps of rock or ore in connection with exploration, evaluation, and development of the Property and other property jointly explored, evaluated or developed; and

(iii) erect, construct, use and maintain on the Property such roads, impoundments, pipelines, wells, power lines, facilities, buildings, structures, machinery and equipment as Homestake may require for the conduct of its operations on the Property or other property jointly explored, evaluated or developed.

-4-

(iv) Homestake will use good faith efforts to conduct all of its operations on the Property in a sound and minerlike manner and will comply fully with the provisions of the Workmen's Compensation Laws of the State of Nevada and will carry and maintain adequate and reasonable liability insurance for operations such as those contemplated by Homestake under this Agreement.

(v) Homestake shall during normal business hours and on reasonable notice make available to Pioche-Ely Valley at such place or places and as they are normally maintained by Homestake, all factual (but not interpretive) maps, samples, assays, drill logs, analytical reports, metallurgical reports or studies and other information and data accumulated hereunder, and all records, accounts, and documents in the possession of Homestake or its Affiliates and their agents which pertain to the Property and the Agreement.

(vi) Homestake agrees to defend, indemnify and hold Pioche-Ely Valley harmless from and against any cost, liability, loss, damage, claim,

expense or contribution (including reasonable attorney's fees) including death, personal injury, or damage to property arising out of or related to Homestake's negligence or willful misconduct or violations of law on or in connection with Homestake's activities on the Property including, but not limited to any violation by Homestake of applicable provisions of federal or state law intended to protect the environment.

(vii) Pioche-Ely Valley and its authorized agents who are experienced in mining operations, shall at Pioche-Ely Valley's sole risk and expense have the right to inspect the Property for the purpose of confirming that Homestake is conducting its operations in the manner required by this Agreement. All such inspections shall be made upon reasonable prior notice to Homestake, in a reasonable manner conforming to Homestake's safety rules and regulations, and so as not to interfere with Homestake's operations. Pioche-Ely Valley agrees to defend, indemnify, and hold Homestake harmless from all cost, liability, loss, damage, claim, expense or contribution (including attorneys fees) including death, personal injury, or damage to property arising out of or related to the acts of omissions of Pioche-Ely Valley, its employees, contractors, agents and representatives on the Property. The indemnities in subsection (vi) and this subsection (vii) shall survive termination of this Agreement.

5. Homestake's Option to Purchase.

(a) Promptly after Homestake's execution of this Agreement, Homestake shall pay Owner \$100.00 as the entire and separate consideration for the term of the Option.

(b) Owner hereby grants to Homestake the exclusive and irrevocable option to purchase an undivided 85% interest in the Property, including but not limited

-5-

to any rights resulting from application of Sections 2(e), 6(c) and (d), ("Option") for a total purchase price of \$3,000,000.

(c) Within ten days after the Effective Date, Owner and Homestake shall execute with a disinterested person selected by Homestake ("Depository") escrow instructions in the form attached at Exhibit B and Owner shall sign, acknowledge and deposit with the Depository deeds in the form attached as Exhibits B-1 and B-2 conveying to Homestake 85% of the 100% interest of Pioche-Ely Valley to the Property other than the Poorman Area and 100% of Pioche-Ely Valley's 85% interest in the Poorman Area to be held by the Depository.

(d) Homestake may exercise the Option at any time while this Agreement is in effect by giving Owner notice of its election to do so specifying the effective date of the purchase and by paying to the Depository the purchase price. On the effective date of the purchase, this Agreement shall terminate, except with respect to payment of the purchase price and the representations and warranties of Owner contained herein. The rights and obligations of the parties to each other shall be governed by the deeds and the Joint Venture Agreement as provided in Section 11 below.

(e) Title to the Property acquired by exercise of the Option must vest in Homestake, if at all, within twenty years following the death of the last surviving descendant of Elizabeth II, Queen of the United Kingdom, who is alive on the Effective Date.

6. Maintenance; Modification of Form of Property.

(a) Except as otherwise provided in Section 6(b), during the term of this Agreement, Homestake, unless it sooner terminates this Agreement, shall in Pioche-Ely Valley's name make all payments and perform all acts or other obligations reasonably necessary as provided in Sections 6(b) and 6(c), to maintain in good standing, and to preserve and protect title to the Property, including but not limited to the payment of all property, sales, use, gross receipts, severance, ad valorem, occupation and privilege taxes, net annual proceeds taxes and any other taxes on minerals, mining or the proceeds from mining whether now or later enacted required to be paid, unless contested in good faith.

(b) Unless it terminates this Agreement on or before June 1 or any

year, Homestake shall (i) pay to the United States of America during the term of this Agreement (and promptly provide evidence thereof to Pioche-Ely Valley) such rentals and other fees and (ii) use good faith efforts to perform such additional acts and obligations as are or may be required to maintain each unpatented mining claim then constituting part of the Property in good standing through August 31st of such year in compliance with all applicable federal and state law including but not limited to the

-6-

United States Interior and Related Agencies Appropriations Act of 1993 and the Omnibus Budget Reconciliation Act of 1993. With respect to assessment work or such other acts or obligations performed by Homestake, Homestake shall prepare and file such affidavits, other documents or evidence thereof as are required by state and federal law to maintain such unpatented mining claims and mill sites in good standing through such August 31st. Following execution of this Agreement, Homestake will reimburse Pioche-Ely Valley for the BLM maintenance fees pertaining to the Property paid for the assessment year ending on September 1, 1998, upon submission of appropriate documentation of such payment to Homestake.

(c) If the Mining Law of 1872 should be amended or repealed during the term of this Agreement, Homestake, unless it sooner terminates this Agreement shall use its best efforts to protect the rights or interests of the parties in any unpatented mining claim or mill site then constituting part of the Property and to acquire from the United States of America and maintain in effect rights to explore, develop and mine and otherwise use the ground covered by each such claim and site under such other forms of mineral tenure as may exist under any federal law hereafter enacted. Any such rights, interests, and other forms or mineral tenure obtained with respect to the ground covered by any such claim or site shall be part of the Property for all purposes of this Agreement.

(d) (i) During the term of this Agreement, Homestake may, (1) locate, amend or relocate in the name of Pioche-Ely Valley, any unpatented mining claims or mill sites then constituting the Property, (2) locate in the name of Pioche-Ely Valley, any fractions resulting from such amendments or relocations, (3) abandon any unpatented mining claims(s) for the purpose of locating mill sites and (4) abandon any unpatented mill sites for the purpose of locating mining claims. All rights so acquired by Homestake shall be part of the Property for all purposes of this Agreement.

(ii) During the term of this Agreement, Homestake shall have the right to (1) exchange with or transfer to the United States of America all or any part of any unpatented mining claim or mill site constituting part of the Property for the purpose of acquiring rights to the ground and/or minerals (in the case of mining claims) covered thereby, and (2) convert all or any part of the Property into one or more leases or other forms of mineral tenure pursuant to any federal law hereafter enacted. Any such ground, lease or other form of tenure shall be part of the Property for all purposes of this Agreement.

(iii) At Homestake's request during the term of this Agreement Pioche-Ely Valley shall apply for mining or mill site patents or mining leases or other forms of mineral tenure for some or all of the unpatented mining claims.

(e) Pioche-Ely Valley agrees to cooperate with Homestake and to take such reasonable actions, execute and deliver such reasonable documents, and

-7-

otherwise provide such reasonable assistance as is useful or necessary to permit Homestake to comply with the provisions of this Section 6.

7. Expenditures By Homestake.

(a) (i) On or before the 1st anniversary of the Effective Date Homestake shall be obligated to expend a minimum of \$50,000 on or in connection with exploration of the Property ("Committed Expenditures") consisting of geological, geochemical and geophysical mapping and other investigations such as test drilling. In the event Homestake does not make such Committed Expenditures in a timely manner, then within thirty days following the first anniversary of the Effective Date Homestake shall pay Pioche-Ely Valley the difference between such \$50,000 and the amount actually expended. Committed Expenditures or payment to Pioche-Ely Valley in lieu thereof are a material and

irrevocable obligation of Homestake pursuant to this Agreement and not merely a condition precedent or subsequent. Except as provided in subsection 7(d), failure to make the Committed Expenditures or payments in lieu thereof shall constitute a material breach of this Agreement.

(ii) In addition, Homestake shall and by using reasonable efforts, complete prior to the first anniversary of the Effective Date one drill hole to a depth of approximately 1,500' at a mutually agreeable location in the Poorman Area; provided, however, that if neither Homestake nor Pioche-Ely Valley, or both, have acquired 100% of the outstanding interests in the Poorman Area within 270 days following the Effective Date, the parties shall agree on a different location for such drill hole outside of the Poorman Area. The completion of the drilling of such a hole is an irrevocable obligation and a condition of maintaining this agreement in effect.

(b) In subsequent years while this Agreement remains in effect, Homestake will make on or prior to each anniversary of the Effective Date exploration expenditures ("Expenditures") in the minimum amount of \$50,000 annually. Expenditures are mere conditions to maintaining this Agreement in effect but are not irrevocable obligations.

(c) For purposes of this Agreement Expenditures (and Committed Expenditures) shall include all amounts paid or incurred by Homestake, whether on or off the Property, in connection with evaluation, exploration or development of the Property. The term shall include, but shall not be limited to: all amounts paid, incurred or accrued in good faith by or on behalf of Homestake in connection with: (i) acquisition of additional rights or interests in the Property; (ii) searching title and curing title defects; (iii) assessment work and/or the cost of claim maintenance rental fees in lieu of assessment work, real property taxes and all other holding costs, but specifically excluding the payments to Pioche-Ely Valley set forth in Section 8 below; (iv) acquisition of public and private permits and authorizations required for operations in connection with the Property, including all bonds and deposits to secure or maintain

-8-

such permits or authorizations; and (v) should Homestake pay or incur costs and expenses of any kind or character, however denominated, in connection with other properties in which Pioche-Ely Valley has no interest, such as easements, access roads, water and electric transmission lines and other rights and facilities useful in connection with the Property, a reasonable allocation of such costs and expenses as Homestake may determine in good faith to be of benefit or potential benefit to the Property.

(d) In the event Homestake does not in any one or more calendar years while this Agreement remains in effect make on or prior to the relevant anniversary of the Effective Date, the relevant minimum Expenditures specified for such year, then in order to continue this Agreement in effect, Homestake shall within thirty days following such anniversary pay to Pioche-Ely Valley the difference between such minimum Expenditure and the amount actually expended. If Homestake does not make such payment in a timely manner this Agreement shall terminate.

(e) Any Expenditures in excess of the minimum required for a particular calendar year shall be credited to Expenditures for one or more subsequent years.

8. Payments By Homestake.

As a condition of continuing this Agreement in effect:

(a) Promptly after Homestake's execution of this Agreement Homestake shall pay Owner \$50,000.00; and,

(b) Or before each anniversary of the Effective Date while this Agreement remains in effect, Homestake shall pay Owner \$50,000.00.

9. Reports By Homestake. Homestake shall from time to time, but not less frequently than annually, give Pioche-Ely Valley a written report of its activities under this Agreement including, but not limited to, a summary of Expenditures as well as copies of all geologic data (but not including interpretations thereof) not previously provided to Pioche-Ely Valley. Homestake and Pioche-Ely Valley will meet not less frequently than annually to

review and discuss the results of the exploration to date. Upon the prior request of Pioche-Ely Valley, Homestake shall provide Pioche-Ely Valley with copies of geologic data (but not including interpretations thereof) at least ten days prior to any meeting. The amount of Expenditures reported in each such report shall conclusively be deemed to be correct unless Pioche-Ely Valley provides written notice to Homestake of its objection and the detailed grounds on which it is based within 60 days after Pioche-Ely Valley's receipt of each such report. Pioche-Ely Valley shall have reasonable access at all times to the books, accounts and records of Homestake to verify and audit the type and amounts of Expenditures made by

-9-

Homestake to qualify under this Agreement. Any such audit shall be requested within 60 days following delivery of the annual report to Pioche-Ely Valley and Pioche-Ely Valley shall be limited to one such audit per calendar year.

10. Data. Upon execution of this Agreement Pioche-Ely Valley will allow Homestake to review and copy all engineering and geologic data in its possession pertaining to the Property.

11. Joint Venture Agreement.

Upon Homestake's exercise of the Option to Purchase and payment of the purchase price as provided in Section 5, Homestake's 85% undivided interest as a tenant-in-common in the Property shall have irrevocably vested in Homestake, the Depository shall record and deliver to Homestake the two deeds referred to in Section 5(c), and Pioche-Ely Valley and Homestake shall become Participants in a Joint Venture ("Joint Venture") on the terms and conditions contained in the Joint Venture Agreement attached hereto as Exhibit C, and this Agreement shall terminate except as otherwise expressly provided herein. Within 15 days following Homestake's vesting in its interest in the Property it shall execute two copies of the Joint Venture and deliver the same to Pioche-Ely Valley for signature. Pioche-Ely Valley shall execute both copies of the Joint Venture and return one fully executed copy to Homestake within 15 days following its receipt thereof. In any event whether or not the Joint Venture has been executed by the parties hereto the Joint Venture shall be effective upon Homestake's vesting in its interest in the Property and for all purposes shall be a valid and enforceable contract. For the avoidance of doubt, in the event that Pioche-Ely Valley has no right, title, or interest in the Poorman Area at the time of such vesting by Homestake, the Poorman Area shall not be an asset of the Joint Venture contemplated by Section 11.

12. Term and Termination.

(a) This Agreement shall terminate on the earliest to occur of (i) the 7th anniversary of the Effective Date if Homestake has not then exercised the Option as provided in Section 5(d), (ii) exercise of the Option as provided in Section 5, or (iii) termination by Homestake pursuant to Section 12(b).

(b) Homestake may terminate this Agreement as to all or any part of the Property at any time after it has completed the Committed Expenditures and prior to exercise of the Option on 60 days written notice of termination to Pioche-Ely Valley.

(c) Upon termination as provided in Section 12(a), (other than a termination arising out of exercise of the Option) Homestake shall execute and deliver to Pioche-Ely Valley such instruments of assignment, transfer and conveyance in customary form as reasonably effect such termination and transfer and (ii) except as

-10-

otherwise required by Section 12(d) any obligation of Homestake contained in or arising out of this Agreement not then due or accrued (express or implied) shall terminate with respect to such portion of the Property as to which this Agreement is terminated.

(d) Upon any complete or partial termination of this Agreement Homestake shall promptly perform all work required to reclaim from the effects of activities carried out by Homestake pursuant to this Agreement to the extent then required by law upon such portion of the Property as to which this Agreement is terminated.

13. Force Majeure.

(a) If Homestake shall be prevented by Force Majeure from timely performance of any obligations arising under this Agreement except the payment of money to third parties, the failure shall be excused and the period for performance shall be extended for a period equal to the duration of Force Majeure. Homestake shall promptly give Pioche-Ely Valley notice of commencement and termination of Force Majeure. Homestake shall use reasonable diligence to remove Force Majeure but shall not be required against its will to institute legal proceedings, adjust any labor dispute or challenge the validity of any law, regulation, action or inaction of government.

(b) "Force Majeure" includes any cause beyond Homestake's reasonable control, whether or not foreseeable, including but not limited to: law, regulation, action or inaction of government; inability to obtain in a timely manner and on terms reasonably acceptable to Homestake any public or private license, permit or authorization which may be required for operations in connection with the Property or other property, including removal and disposal of waters, wastes and tailings and reclamation; fire; explosion; inclement weather; flood; civil commotion; labor dispute; inability to obtain workmen or material; delay in transportation; and acts of God.

14. Notices. All notices and other communications to either party shall be in writing and delivered personally or sent by prepaid mail, telecopier or other means providing for receipt of the communication in written form. All notices of default or arbitration and demands for performance or assurance, may be delivered personally or, if mailed, shall be sent by certified or registered mail, return receipt requested. Notices sent by ordinary mail shall be effective five days after the date of mailing. Notices sent by certified or registered mail shall be effective on the next business day after the date of actual delivery. Notices sent by telecopier shall be effective on the next business day after the day of transmission. Until a change of address is so given, notices shall be addressed to Homestake and Pioche-Ely Valley, respectively.

-11-

Homestake:

Homestake Mining Company of California
650 California Street, 11th Floor
San Francisco, California 94108
Attn: Senior Land Manager
Telephone: (415) 981-8150
Fax: (415) 397-5025

with a copy to:

Homestake Mining Company of California
605 Boxington Way, Suite 112
Sparks, Nevada 89434
Attn: Land Manager, U.S.
Telephone: (702) 358-5609
Fax: (702) 358-5588

Pioche-Ely Valley:

Pioche-Ely Valley Mines, Inc.
10830 N. Central Expressway, Suite 175
Dallas, Texas 75231
Attn:
Telephone: (214) 692-7872
Fax: (214) 692-7874

15. Assignment; Right of First Refusal.

(a) Subject to the conditions of this Section 15, either party may assign all (but not less than all) of its interest in this Agreement or the Property (i) to an Affiliate or (ii) to a person or entity that is not an Affiliate after obtaining the prior written consent of the other which shall not be unreasonably withheld; provided in all cases, however, that the proposed assignee shall first agree in writing for the benefit of the non-assigning party to be bound by the terms and condition of this Agreement.

(b) If either party intends to assign its interest in this Agreement

or the Property to other than an Affiliate, the party proposing the assignment shall first deliver written notice of such intent to the non-assigning party. The non-assigning party shall have the right to negotiate at arms-length the acquisition of the interest to be assigned. If within sixty days no agreement has been made between the parties, then the assigning party may enter into negotiations with third parties.

-12-

(c) If either party intends to assign its interest in this Agreement or the Property to other than an Affiliate, the non-assigning party shall have the right of first refusal. The party proposing to assign its interest shall provide the non-assigning party written notice of the pertinent terms and conditions of the offer of the third party and the proposed assignment including all documents containing the offer. The non-assigning party shall have thirty days from the date such notice is delivered to notify the assigning party whether it elects to acquire the offered interest at the same price and on the same terms and conditions as set forth in the notice. In the event any consideration to be paid pursuant to a third party offer is not in US dollars, the non-assigning party shall have the right to substitute for such consideration the fair market value thereof in US dollars as agreed upon by the parties or as determined by arbitration pursuant to Section 20. In the event the non-assigning party does not exercise its right of first refusal, the assigning party shall have 60 days to complete the assignment on the terms and conditions contained in the notice to the non-assigning party after which 60 days the right of first refusal of the non-assigning party shall once again apply.

16. No Environmental and Reclamation Liability. Notwithstanding any other provision of this Agreement, Homestake shall have no liability or obligation of any kind to Pioche-Ely Valley or to any third party for the reclamation or remediation of any environmental or other condition on or relating to the Property arising from any exploration, mining activities or other activity or use of the Property prior to the Effective Date. Pioche-Ely Valley agrees to defend, indemnify, and hold Homestake, its Affiliates and their directors, officers, employees, and representatives harmless from any cost, liability, loss, damage, claim, expense or contribution, including attorneys fees, arising from or related to any such condition or the reclamation or remediation thereof arising from or relating to activities conducted prior to the Effective Date. In the event Homestake exercises the Option to Purchase contained in Section 5 then Homestake shall assume and shall be obligated to pay its respective proportionate amounts of reclamation and remediation costs arising from any exploration, mining activities or other activity or use of the Property regardless of when such activity took place.

17. Confidentiality of Information; Press Releases. Except as otherwise provided in this Section 17, Pioche-Ely Valley shall treat all data, reports, records and other information relating to this Agreement and the Property confidential. Each party shall be free to issue press releases and make public announcements with respect to this Agreement or the transactions contemplated by it but before doing so shall afford the other a reasonable opportunity to review and comment on them. Neither party shall issue any release or announcement that includes the name of the other without receiving the other's written consent, which consent shall not be unreasonably withheld, conditioned or delayed.

18. Termination of Confidentiality Agreement. That certain confidentiality agreement between Pioche-Ely Valley Mines, Inc. and Homestake Mining Company of California dated January 31, 1997 is hereby terminated.

-13-

19. SHORT FORM; RECORDATION. The parties agree to execute and Homestake agrees to record a short form of this Agreement in order to provide notice of it to third parties. Homestake may record this Agreement, the short form, or both.

20. ARBITRATION. Any disagreement or dispute arising out of this Agreement, its existence, interpretation, performance or enforcement not resolved by the disputing parties within fifty days from the date on which any party notifies one or more of the others of any such disagreement or dispute shall be decided finally by arbitration before three arbitrators in Reno, Nevada under the Commercial Arbitration Rules of the American Arbitration Association. Such notice shall appoint one arbitrator. Within ten days of the receipt of such notice, the other party shall appoint a second arbitrator and

the two arbitrators so named shall within ten days of the appointment of the second appoint the third. If the two arbitrators appointed cannot agree upon the third arbitrator within such ten days, either party may apply to the Chief Judge of the United States District Court of the District including Reno to designate the third arbitrator. Each arbitrator shall be an individual qualified by skill and experience in the subject matter under dispute. No discovery shall be available. Each party shall bear its own costs in the arbitration. Each arbitrating party shall bear the costs of the arbitrator appointed by such party and the costs of the third arbitrator shall be borne equally by all of the arbitrating parties. The arbitrators shall enter their award within 45 days following the appointment of the third arbitrator. The award shall be binding on each of the arbitrating parties and its Affiliates and may be enforced in any court having jurisdiction over the person or property of any person against whom enforcement of the award is sought.

21. GOVERNING LAW. The existence, interpretation, performance, discharge, excuse, waiver, breach and termination of this Agreement shall be governed by the domestic law of the State of Nevada.

22. AREA OF INTEREST. Each party acknowledges that except as provided in Section 3(d) and in Section 23, this Agreement contains no area of interest or other limitation or restriction on the rights of the parties to acquire property adjacent to or nearby the Property for their own account or to otherwise engage in business for their own accounts or whether not competitive with activities of the other.

23. ADDITIONAL AND AFTER-ACQUIRED RIGHTS. If Pioche-Ely Valley acquires and right or interest in the Property or within the outer boundaries of the Property while this Agreement is in effect, (i) Pioche-Ely Valley shall promptly notify Homestake, (ii) such right or interest shall automatically become part of the Property for purposes of the Agreement, and (iii) Pioche-Ely Valley shall sign, acknowledge and deliver to Homestake an amendment to this Agreement and any memorandum of this Agreement so as to include such right or interest as part of the Property

-14-

24. ENTIRE AGREEMENT. (a) This Agreement contains the entire agreement and understanding between the parties related to its subject matter and supersedes any prior and contemporaneous agreements, commitments, representations, writings and discussions relating thereto, whether written or oral, express or implied, all of which are hereby terminated in their entirety as of the date of this Agreement. The parties have endeavored to express in this Agreement all consideration, warranties, representations, and covenants that they intend, this Agreement shall not be construed to contain any implied consideration, warranties, representations, or covenants, including but not limited to any implied obligation of Homestake to explore, mine or otherwise work the Property and is not intended to create any partnership between the parties.

(b) The parties agree that they will execute such further agreements, conveyances and assurances as may be required or which counsel for the parties may deem necessary to carry out the intent of this Agreement.

(c) This Agreement shall inure to the benefit of and be binding upon the parties hereto and their respective successors and assigns.

Homestake Mining Company of California

Pioche-Ely Valley Mines, Inc.

By: /s/ W.F. LINDQUIST

By: /s/ J.A. CRICHTON

Print Name: W.F. Lindquist

Print Name: J.A. Crichton

Title: Vice President

Title: President

EXHIBIT A

The Property consists of those certain patented and unpatented mining claims located generally in Township 1 North, Ranges 66 and 67 East, Lincoln County, Nevada, and more particularly described as follows:

PART I.

A. PATENTED CLAIMS

<TABLE>

<CAPTION>

CLAIM NAME	MINERAL SURVEY NO.	PATENT NO.
<S>	<C>	<C>
Daly East	2526	46548
Key Note	3180	83147
Lucky Boy	3180	83147
Imperial	3181	84930
Iron Duke	3181	84930
Double Decker	3183	74644
Columbia	3183	74644
Commander	3182	77977
Dupont No. 1	3820	441200
Volcano	4305	646889
Buckhorn	4185	496585
Buckhorn No. 2	4185	496585
Deertrail	4185	496585
Jonathan	4185	496585
Jonathan No. 2	4185	496585
Rawhide	4185	496585
Smuggler	4185	496585
Gelder	4160	504310
Gelder No. 2	4160	504310
West End	4160	504310
Start Up	4160	504310
Start Up No. 2	4160	504310
Gold Eagle No. 3	4160	504310
Gold Eagle No. 4	4160	504310
Gold Eagle Consolidated	4160	504310
Hard Road	4160	504310

</TABLE>

Exhibit A - Page 1

<TABLE>

<S>	<C>	<C>
Ely Valley	3725	221093
Ely Valley No. 2	3725	221093
Ely Valley No. 3	3725	221093
Ely Valley No. 4	3725	221093
Ely Valley No. 5	3725	221093
O.K.	3725	221093
Alice	3725	221093
Golden Fleece	3725	221093
Margaret Pillins	3725	221093
Silver Dick	3864	245094
Annice	3864	245094
Jefferson	3864	245094
Baby Mine Fraction	3864	245094
Ophir	4072	339883
Flagstaff	4072	339883
Navy	2153A	34618
Melissa	38	31074

</TABLE>

PART I.B. UNPATENTED CLAIMS

<TABLE>
<CAPTION>

CLAIM NAME	LOCATION DATE	BOOK/PAGE	BLM NMC #
<S>	<C>	<C>	<C>
Army	1/13/1900	L/227	80347
Battery	2/12/1900	L/323	80348
Northside	2/12/1900	L/325	80349
Mendha	1/8/1900	L/218	80350
North Side No. 2	5/17/1909	D-1/35	80351
Navy West	1/29/1900	L/262	80352
Southside	3/7/1900	L/326	80353
Southside No. 1	5/20/1909	D-1/35	80354
Mendha East	1/8/1900	L/220	80355
Northside No. 1	5/16/1909	D-1/34	80356
Wide Awake	10/26/1907	Y/122	80370
Golden Wren	3/4/1907	W/37	80373
Dupont No. 4	7/27/1909	D-1/16	80376
Dupont Fraction No. 3	2/11/1907	V/137	80377
Nail Driver	11/12/1906	U/372	80378
Superior No. 1	9/27/1922	G-1/260	80385

</TABLE>

EXHIBIT A - PAGE 2

<TABLE>

<S>	<C>	<C>	<C>
Superior No. 2	9/27/1922	G-1/260	80386
Harvester No. 2	11/20/1927	H-1/272	80390
Harvester No. 3	5/23/1940	M-1/345	80391
Harvester No. 42	5/11/1946	N-1/440	80430
O.K. No. 2	5/20/1929	H-1/466	80431
O.K. No. 3	1/25/1907	W/90	80432
O.K. No. 4	9/23/1907	Y/211	80433
O.K. No. 5	5/9/1929	H-1/475	80434
O.K. No. 7	5/9/1929	H-1/475	80436
Marion	1/28/1918	F-1/227	80450
Marion No. 2	2/2/1918	F-1/227	80451
Marion No. 3	9/12/1929	J-1/164	80452
Marion No. 4	9/12/1929	J-1/165	80453
Marion No. 7	9/13/1929	J-1/166	80456
Blue Bell No. 1	1/11/1911	E-1/15	80457
Blue Bell No. 2	1/11/1911	E-1/15	80458
Blue Bell No. 3	1/11/1911	E-1/16	80459
Blue Bell No. 4	1/11/1911	E-1/16	80460
Blue Bell No. 5	7/1/1931	K-1/117	80461
Blue Bell No. 6	7/1/1931	K-1/118	80462
Blue Bell No. 7	7/1/1931	K-1/118	80463
Blue Bell No. 8	7/1/1931	K-1/119	80464
Sure Thing	6/24/1926	H-1/95	80465
Sure Thing No. 1	8/17/1926	H-1/96	80466
Sure Thing No. 2	8/17/1926	J-1/167	80467
Blue Bell No. 10	7/1/1931	K-1/119	80477
Blue Bell No. 11	10/8/1935	L-1/89	80478
Blue Bell No. 12	10/8/1935	L-1/89	80479
Blue Bell No. 13	10/8/1935	L-1/90	80480
Blue Bell No. 14	10/9/1935	L-1/90	80481
Blue Bell No. 15	10/9/1935	L-1/91	80482
Harebell	9/13/1993	107/256	681915
Cathy Fraction	9/7/1993	107/254	681916
Anne Fraction	10/26/1987	77/464-465	443772
Joyce Fraction	10/3/1987	77/474-475	443777
Telex	11/4/1987	77/494-495	443787

</TABLE>

EXHIBIT A - PAGE 3

PART II. POORMAN AREA

A. PATENTED CLAIMS

<TABLE>
<CAPTION>

CLAIM NAME	MINERAL SURVEY NO.	PATENT NO.
<S>	<C>	<C>
Jig	57	28391
Youngatti	57	28391
Capen	57	28391
Albion	57	28391
Poorman's Prospect	57	28391

</TABLE>

B. UNPATENTED CLAIMS

<TABLE>
<CAPTION>

CLAIM NAME	LOCATION DATE	BOOK/PAGE	NMC #'S
<S>	<C>	<C>	<C>
September	10/2/1929	J-1/204	80357
Acme	5/30/1928	H-1/321	80358
Acme No. 2	5/30/1928	H-1/321	80359
Acme No. 3	5/30/1928	H-1/321	80360
Acme No. 4	5/30/1928	H-1/322	80361
Acme No. 5	3/25/1928	H-1/322	80473
Acme No. 6	3/25/1928	H-1/323	80474
James No. 1	9/1/1939	M-1/194	80362
James No. 2	9/1/1939	M-1/194	80363
James No. 3	9/1/1939	M-1/195	80364
James No. 4	8/6/1940	M-1/379	80365
James No. 5	8/6/1940	M-1/379	80366
James No. 6	8/6/1940	M-1/380	80367
James No. 7	8/6/1940	M-1/380	80368
Garbo #23	4/20/1990	91/45	597895

</TABLE>

EXHIBIT A - PAGE 4

<TABLE>

<S>	<C>	<C>	<C>
Garbo #24	4/20/1990	91/46	597896
Garbo #25	4/20/1990	91/47	597897
Garbo #26	4/20/1990	91/48	597898
Garbo #27	4/20/1990	91/49	597899
Garbo #28	4/20/1990	91/50	597900
Garbo #29	4/20/1990	91/51	597901
Garbo #30	4/20/1990	91/52	507902
Garbo #31	4/20/1990	91/53	597903
Garbo #49	4/25/1990	91/71	597921
Garbo #50	4/25/1990	91/72	597922
Garbo #52	4/25/1990	91/73	597923
Garbo #53	4/25/1990	91/74	597924
Garbo #54	4/25/1990	91/75	597925
Garbo #55	4/25/1990	91/76	597926
Garbo #56	4/26/1990	91/77	597927

</TABLE>

EXHIBIT A - PAGE 5

AMENDMENT NO. 1 TO AMENDED AND RESTATED CREDIT AGREEMENT

THIS AMENDMENT NO. 1 TO AMENDED AND RESTATED CREDIT AGREEMENT ("Amendment No. 1") is made and entered into as of the 31st day of December, 1997, by and between South Hampton Refining Company, a Texas corporation (the "Borrower") and Den norske Bank ASA, New York Branch, a Norwegian bank (the "Bank").

For and in consideration of the mutual covenants and agreements herein contained, Borrower and Bank hereby amend as of the date of this Agreement that certain Amended and Restated Credit Agreement between the Borrower and the Bank dated October 15, 1996 (the "Credit Agreement") in the following respects:

Section 1. Amendment to Credit Agreement.

(a) The definition of "Maturity Date" in the Credit Agreement is hereby amended to read as follows:

"Maturity Date" means December 31, 1999 or as extended in the sole discretion of the Bank.

Section 2. Closing. The closing of the transactions contemplated by this Amendment No. 1 is subject to the satisfaction of the following conditions.

2.1 Counsel to Lender. All legal matters incident to the transactions herein contemplated shall be satisfactory to Gardere Wynne Sewell & Riggs, L.L.P., counsel to the Bank.

2.2 Required Documents. The Bank shall have received fully executed copies of (i) this Amendment No. 1, (ii) the Endorsement No. 1 to Promissory Note, (iii) the Ratification of Security Agreement, (iv) the Ratification of Assignment of Insurances, (v) the Ratification of Pledge, and (vi) the Notice of Final Agreement.

Section 3. Ratification. Except as amended hereby, the Credit Agreement shall remain unchanged and the terms, conditions, representations, warranties, and covenants of said Credit Agreement are true as of the date hereof, are ratified and confirmed in all respects and shall be continuing and binding upon the parties.

Section 4. Defined Terms. All terms used in this Amendment No. 1 which are defined in the Credit Agreement shall have the same meaning as in the Credit Agreement, except as otherwise indicated in this Amendment No. 1.

Section 5. Multiple Counterparts. This Amendment No. 1 may be executed by the parties hereto in several separate counterparts, each of which shall be an original and all of which taken together shall constitute one and the same agreement.

Section 6. Applicable Law. This Amendment No. 1 shall be deemed to be a contract under and subject to, and shall be construed for all purposes in accordance with the laws of the State of Texas.

Section 7. Final Agreement. THE WRITTEN CREDIT AGREEMENT IN CONNECTION WITH THIS AMENDMENT NO. 1 REPRESENTS THE FINAL AGREEMENT BETWEEN THE BORROWER AND THE BANK AND MAY NOT BE CONTRADICTED BY EVIDENCE OF PRIOR, CONTEMPORANEOUS, OR SUBSEQUENT ORAL AGREEMENTS OF THE BORROWER AND THE BANK. THERE ARE NO UNWRITTEN ORAL AGREEMENTS BETWEEN THE BANK AND THE BORROWER.

IN WRITTEN WHEREOF, the parties have caused this Amendment No. 1 to be executed by their duly authorized officers as of the 31st day of December, 1997.

By: /s/ NICHOLAS CARTER

Nicholas Carter
President

DEN NORSE BANK ASA,
NEW YORK BRANCH

By: /s/ BYRON L. COOLEY

Byron L. Cooley
Senior Vice President

By: /s/ MORTEN BJORNSEN

Morten Bjornsen
Senior Vice President

-2-

ENDORSEMENT NO. 1

Endorsement No. 1 dated as of December 31, 1997 to the Promissory Note dated October 15, 1996 (the "Note") in the principal amount of USD 1,965,000 from SOUTH HAMPTON REFINING COMPANY, a Texas corporation (the "Borrower") in favor of DEN NORSE BANK ASA , NEW YORK BRANCH, a Norwegian bank (the "Bank").

The Note is hereby amended, effective the date hereof, as follows:

1. The maturity date of the Note is hereby changed to December 31, 1999 wherever it appears.

2. Wherever and in each place the term "Note" is used in the Note, it shall be read to mean the Note as amended by this Endorsement No. 1. Except as specifically amended by this Endorsement No. 1, all of the terms of the Note shall continue in full force and effect.

3. No temporary waiver or forbearance by the payee of any provision of the Note whether evidenced by this Endorsement No. 1 or otherwise shall bind the payee to grant any further waivers or forbearances.

IN WITNESS WHEREOF, the parties hereto have executed this Endorsement No. 1 the day and year first above written.

SOUTH HAMPTON REFINING COMPANY

By: /s/ NICHOLAS CARTER

Nicholas Carter
President

DEN NORSE BANK ASA,
NEW YORK BRANCH

By: /s/ BYRON L. COOLEY

Byron L. Cooley
Senior Vice President

By: /s/ MORTEN BJORNSEN

Morten Bjornsen
Senior Vice President

[Signature Page -- Endorsement No. 1]

ARABIAN SHIELD
DEVELOPMENT COMPANY

ANNUAL REPORT TO STOCKHOLDERS
FOR THE YEAR ENDED DECEMBER 31, 1997

TO OUR STOCKHOLDERS:

The Company obtained the mining lease to the Al Masane area in Saudi Arabia on May 22, 1993, and thereafter commissioned Watts, Griffis & McOuat Limited of Toronto, Canada ("WGM") to update the feasibility study for that area, which was subsequently updated in 1996. The mining lease has an initial thirty (30) year term, with the Company having the option to renew or extend the term of the lease for additional periods not to exceed twenty (20) years. The Company will pay the Saudi Arabian government income taxes in accordance with the income tax law then in force, in accordance with Article 45 of the Mining Code (the current tax is now 45% of net income). However, in accordance with Article 46 of the Mining Code, such income tax will not be due in respect to mining operations during the period of five years starting from the date of the first sale of products or five years from the beginning of the fourth year after the issue of the mining lease, whichever occurs first.

In the 1996 update to the 1994 full bank feasibility study of the Al Masane lease area, the independent mining consultants estimated the total capital costs of the Al Masane project to be \$88.6 million. The Company and its Saudi Arabian advisors are in the process of forming a Saudi limited liability company to own and operate the project. On November 5, 1997, the Company and the Al Mashreq Company for Mining Investments ("Al Mashreq"), a Saudi limited liability company owned by Saudi Arabian investors, initialed a joint venture agreement to form a Saudi limited liability company which will be owned 50% by the Company and 50% by Al Mashreq. The new company, called "The Arabian Shield Company for Mining Industries Ltd.", is now under formation and has applied to the Saudi Ministry of Commerce for a charter to operate the mine.

The Company believes that 25% of the capital cost of the project may be obtained through loans from commercial banks, 50% of the capital cost of the project would come from an interest-free loan from the Saudi Industrial Development Fund ("SIDF") and that Saudi Arabian investors will contribute the remaining 25% of the capital cost of the project. A loan application was submitted to SIDF on September 30, 1995 and conditional approval was received on December 17, 1997 for a \$38.08 million loan. In order to be eligible for the interest-free loan from the SIDF, the Company together with its Saudi Arabian advisors obtained an industrial license from The Ministry of Industry and Electricity on December 3, 1996. The license was amended to reflect the transfer from the two Saudi Arabian advisors to Al Mashreq on November 22, 1997. The Company owns 50% of the license and Al Mashreq the remaining 50%. Under the mining lease agreement, when actual profits are realized from commercial mining operations of the project, it is contemplated that the Saudi limited liability company will be transformed into a Saudi public stock company. The Company and Al Mashreq will own no less than 50% of the shares, the Petroleum and Mineral Organization ("Petromin"), a company wholly owned by the Saudi Arabian government, will have the option to acquire up to 25% of the shares, and the remaining shares will be offered for public subscription to Saudi Arabian citizens.

Pursuant to the terms of the mining lease agreement, the Company will undertake to repay the \$11 million loan provided to the Company in 1979 by the Ministry of Finance and National Economy, in accordance with the terms of an agreement to be negotiated between the Company and the Ministry of Finance and National Economy. In a memorandum to His Majesty the King in 1986, the Minister of Petroleum and Mineral Resources and the Minister of Finance and National Economy recommended that the \$11 million loan be rescheduled with the terms of rescheduling to be agreed upon after the mining lease is granted. The Company will instigate negotiations on that basis with the Ministry of Finance and National Economy.

Under the terms of the mining lease agreement, the Company agreed to pay advance rentals to the Ministry of Petroleum and Mineral Resources of 10,000 Saudi Riyals (approximately \$2,667 at current exchange rate) per square kilometer per year (approximately \$117,300 annually) during the period of the lease for the total lease area of 44 square kilometers. The Company has made all rental payments under the lease.

Following the granting of the mining lease to the Al Masane area, the Company commissioned WGM to prepare a new fully bankable feasibility study for presentation to financial institutions in connection with

obtaining financing for the project. The feasibility study includes more metallurgical work incorporating advances in grinding of the ore; incorporation of the latest advances in technology and reagents developed during the past ten years; incorporation of new mill designs and the latest water recycling methods; investigation into the shipping and marketing of zinc and copper concentrates; and an economic analysis of the project. The feasibility study contains specific recommendations to insure that the construction of the project is accomplished as expeditiously and economically as possible. Engineering design and costing of the project was done by Davy International of Toronto, Canada. The feasibility

study cost the Company approximately \$1 million and was presented to the Company on July 22, 1994. The feasibility study was updated in July 1996.

The Al Masane ore is located in three mineralized zones known as Saadah, Al Houra and Moyeath. The diluted minable, proven and probable ore reserves at the Al Masane project were estimated to be 7.2 million tonnes, including mining dilution. Mining dilution is the amount of wallrock adjacent to the ore body which is included in the ore extraction process. The average grade of the proven and probable diluted ore reserves was estimated to be 1.42% copper, 5.31% zinc, 1.19 grams of gold per tonne and 40.20 grams of silver per tonne. For purposes of calculating the proven and probable reserves, a dilution of 5% at zero grade on the Saadah zone and 15% at zero grade on the Al Houra and Moyeath zones was assumed. A mining recovery of 80% has been used for the Saadah Zone and 88% for the Al Houra and Moyeath Zones.

A review by WGM of the equipment and process flowsheet contained in the 1982 feasibility study prepared by WGM indicated that new technology developed during the past ten years could be used to reduce the capital cost and improve the metallurgical recoveries. In particular, the use of semi-autogenous grinding to reduce the capital cost of the grinding section and developments in reagents were believed to hold the greatest potential for improving the economies of the project. A detailed metallurgical testwork program was undertaken by Lakefield Research in 1994 to address potential improvements and provide detailed design criteria for the concentrator design. Results from this testwork program showed that copper recovery could be improved by 5.7% and zinc recoveries improved by 13% compared to the 1982 results.

The metallurgical studies conducted on the ore samples taken from the zones indicated that 87.7% of the copper and 82.6% of the zinc could be recovered in copper and zinc concentrates. Overall, gold and silver recovery from the ore was estimated to be 77.3% and 81.3%, respectively, partly into copper concentrate and partly as bullion through cyanide processing of zinc concentrates and mine tailings.

A test program to evaluate the economies of the cyanidation of the zinc concentrate and tailings in order to improve gold and silver recoveries found gold and silver recoveries to range from 50% to 77%. To recover gold and silver from the zinc concentrate and tailings, WGM recommended that a cyanidation plant be included in the process flowsheet. Dore bullion would be produced. WGM concluded that the inclusion of a cyanidation plant would make a positive contribution to the economies of the project under the base conditions.

The mining and milling operation recommended by WGM for Al Masane would involve the production of 2,000 tonnes of ore per day (700,000 tonnes per year), with a mine life of over ten years. Annual production is estimated to be 34,900 tonnes of copper concentrate (25% copper per tonne) containing precious metal and 58,000 tonnes of zinc concentrate (54% zinc per tonne). Total output per year of gold and silver is estimated to be 22,000 ounces of gold and 800,000 ounces of silver from the copper concentrate and bullion produced. The construction of mining, milling and infrastructure facilities is estimated to take 18 months to complete. Construction necessary to bring the Al Masane project into production includes the construction of a 2,000 tonne per day concentrator, infrastructure with a 300 man housing facility and the installation of a cyanidation plant to increase the recovery of precious metals from the deposit. Project power requirements will be met by diesel generated power.

WGM recommended that the Al Masane reserves be mined by underground methods using trackless mining equipment. Once the raw ore is mined, it would be subjected to a grinding and treating process resulting in three products to be delivered to smelters for further refining. These products are zinc

2

concentrate, copper concentrate and dore bullion. The copper concentrate will contain valuable amounts of gold and silver. These concentrates are estimated to be 22,000 ounces of gold and 800,000 ounces of silver and will be sold to copper and zinc custom smelters and refineries worldwide.

In the feasibility study, WGM states that there is potential to find more reserves within the lease area, as the ore zones are all open at depth. Further diamond drilling, which will be undertaken by the Company, is required to quantify the additional mineralization associated with these zones. A significant feature of the Al Masane ore zones is that they tend to have a much greater vertical plunge than strike length; relatively small surface exposures such as the Moyeath zone are being developed into sizeable ore tonnages by thorough and systematic exploration. Similarly, systematic prospecting of the small gossans in the area could yield significant tonnages of new ore.

WGM prepared an economic analysis of the project utilizing cash flow projections in the 1996 update of the feasibility study. A base case was prepared that included those project elements which are most likely to be achieved. WGM believed that a majority of the base case assumptions used in the 1994 feasibility study remained valid, including the ore reserves, mill feed grade, production rate, metal recoveries and concentrate grade and smelter returns. Metal prices, capital costs, operating costs and the corporate structure were adjusted to reflect more current information. Capital and operating costs were adjusted in conformity with the updated estimates prepared by Davy International.

The base case assumes the corporate structure of the entity to be formed to operate the project, currently planned to be a Saudi limited liability company, will be owned 50% by the Company and 50% by Saudi Arabian investors and that the owners of this entity would contribute an aggregate of \$21.2 million to the cost of the project. The base case further assumes financing for the project from commercial loans in the aggregate amount of \$21.2 million bearing interest at the rate of 8% per year and a loan in the amount of \$43.8 million from the SIDF repayable in equal annual installments over the initial life of the mine. The remainder of the project financing would be contributed by cash generated by the operation of the project. The base case assumes that the \$11 million loan outstanding to the Saudi Arabian government will be paid by the Company in accordance with a repayment schedule to be agreed upon with the Saudi Arabian government. Based on these assumptions, and assuming the average prices of metal over the life of the mine to be \$1.05 per pound for copper, \$.60 per pound for zinc, \$400 per ounce of gold and \$6.00 per ounce of silver, WGM's economic analysis of the base case shows the project will realize an internal rate of return of 13.1%, the Company's and the Saudi Arabian investors' internal rates of return would be 27.3% and 12.1%, respectively, and projected net cash flow from the project of \$95.1 million. The 1994 feasibility study base case showed the project would realize a 14.05% internal rate of return. Cash flow under the base case is exclusive of income tax as the base case assumes that any such tax would be paid by individual investors and not by the project. Assuming a 10% discount rate, the net present value of the project as shown in the update is \$12.16 million compared to the \$15.5 million net present value of the project shown in the 1994 feasibility study. Based on the update, WGM believes that the economic analysis shows that the project remains viable.

On May 15, 1991, the Company filed a complaint with the U.S. Department of Justice ("DOJ") against Hunt Oil Company of Dallas, Texas ("Hunt"), alleging violations of the Foreign Corrupt Practices Act ("FCPA") by Hunt in obtaining its Petroleum Production Sharing Agreement ("PSA") in Yemen in 1981, subsequent to the Company presenting a bid to the Yemen government for the same area before Hunt made its application. The Company's Washington, D.C. attorneys opined that, because the PSA of Hunt is still ongoing, and under its auspices, payments and receipts occur daily, the DOJ still has jurisdiction to continue its investigation. A letter from the DOJ on December 19, 1995 stated its interest in receiving additional documentation regarding the Company's allegations. On February 28, 1996, the Company sent more documents to the DOJ which it believed further supported its allegations. The Company's Washington, D.C. attorneys opined also that the Victim Restitution Act provides for restitution to the Company of monies lost as a result of the alleged wrongdoing by Hunt, if Hunt is convicted under the FCPA. A letter from the DOJ dated October 1, 1996 stated that the documents presented did not suggest any criminal events occurred within the statute of limitations, and that, at that time, the DOJ did not intend to pursue the investigation. On November 18, 1996, legal counsel retained by the Company,

3

after studying the facts of the case, sent the DOJ an analysis concluding that while the statute of limitations of FCPA may have lapsed, the statute of limitations for conspiracy to violate the FCPA had not lapsed, and that, as a consequence, the DOJ could criminally prosecute Yemen Hunt for conspiracy to violate the FCPA. The Company's legal counsel met with the Fraud Section of the DOJ on December 13, 1996 and were told that the DOJ would take a more aggressive stance if more information of evidentiary quality were presented to the DOJ. The Company intends to vigorously pursue obtaining such further information in the United States and in Yemen.

Late in 1994, articles were published in two prominent Yemen newspapers in which Yemen Hunt Oil Company, a wholly owned subsidiary of Hunt Oil Company of Dallas, Texas ("Yemen Hunt"), was accused of obtaining a petroleum production sharing agreement in Yemen in 1981 through the corruption of Yemen officials in order to exclude the application of the Company and its then partner, Dorchester Gas Company, from consideration for the same area. A letter to the editor of one of these newspapers, published on December 7, 1994 and signed by the executive vice president of Yemen Hunt, after explicitly mentioning the Company and Dorchester Gas Company, stated that "[Yemen Hunt] knows well those suspicious companies who are mainly engaged in political activities for the purpose of undermining the economic interest of Yemen..." On December 26, 1995, the Company filed a complaint of criminal libel with the Yemen Attorney General for Publications in Sana'a, Yemen against Yemen Hunt, alleging that Yemen Hunt, in its published letter to the prominent Yemen newspaper, had criminally libeled the Company, which, if not addressed, could seriously affect the business and reputation of the Company and its employees in the Middle East. In October 1996, the Company received the official decision from the Deputy Attorney General for Publications of Yemen which stated that, after taking the statement of the President of the Company and the statement of the chief of the legal department of Yemen Hunt, it was evident that the letter from Yemen Hunt published in the Yemen newspaper on December 7, 1994 was libelous to the Company. However, since the four month statute of limitations period under Yemen criminal law had run, Yemen Hunt could not be prosecuted for criminal libel. The Company intends to vigorously pursue the matter under the civil libel laws of Yemen.

The Company owns, through a wholly owned subsidiary, South Hampton Refining Company, of Silsbee, Texas which owns and operates a special products refinery which produces pure pentanes and hexanes and other specialty chemicals for the plastics industry. Total gross revenues for 1997 for the refinery operations were approximately \$26.2 million and earnings before interest, taxes and

depreciation and amortization were approximately \$2.2 million. It is significant that the plant sells about 40% of all pentanes consumed in the United States.

4

The Company directly owns approximately 44% and beneficially owns approximately 52% of the outstanding capital stock of Pioche-Ely Valley Mines, Inc. ("Pioche"), an inactive mining company. Pioche's principal assets are a 300 ton per day mill, and 48 patented and 81 unpatented federal lode mining claims in the Pioche Mining District in southeastern Nevada, on which is located the Ely Valley Mine which, between 1941 and 1952, produced 675,207 tons of ore with an average grade of 9.09% zinc. In October 1997, Pioche entered into an Exploration Agreement and Option to Purchase with a large mining company which provides for annual payments to Pioche of \$50,000 for seven years until, or unless, the mining company exercises an option to purchase an 85% interest in the mining claims for \$3 million. The agreement can be terminated upon 60 days written notice from the mining company. The mining company has agreed to expend at least \$50,000 in exploration work each year and to drill at least one hole in the first year.

Respectfully submitted,

John A. Crichton
Chairman of the Board

Hatem El-Khalidi
President and Chief Executive
Officer

March 30, 1998

5

THE COMPANY.

Arabian Shield Development Company (the "Company") was organized as a Delaware corporation in 1967 and is principally engaged in the refining of various specialty petrochemical products and developing various mineral properties. All of its mineral properties are undeveloped and require significant capital expenditures before any commercial operations are commenced. The Company has operations in both the United States and Saudi Arabia. The Company's undeveloped mineral interests are primarily located in Saudi Arabia.

SAUDI ARABIAN ACTIVITIES. The Company holds a mining lease covering a 44 square kilometer area in the Al Masane area in southwestern Saudi Arabia. The lease was granted to the Company by Royal Decree in May 1993. The lease has an initial thirty (30)-year term and is renewable for additional periods not to exceed twenty (20) years. The Al Masane area has proven and probable ore reserves of copper, zinc, gold and silver (7.2 million tonnes of ore containing 1.42% copper, 5.31% zinc, 1.19 grams per tonne of gold and 40.20 grams per tonne of silver). The results of the 1996 update to the 1994 bankable feasibility study conducted by an independent mineral consulting firm indicate that the proposed Al Masane mining operation is economically viable.

The Company was granted exploration licenses for the Wadi Qatan and Jebel Harr areas in southwestern Saudi Arabia, approximately 30 kilometers east of the Al Masane area, in 1971 and 1977, respectively. The exploration licenses by their terms have expired. The Company has been orally advised by Saudi Arabian government officials that the licenses will be extended as long as mineral exploration is being conducted on the areas which they cover, although there can be no assurance that the Company's license rights will be honored. The Company remains a party to an agreement with the Petroleum and Mineral Organization ("Petromin"), the official mining and petroleum company of the Saudi Arabian government, which governs the rights of the parties if an exploration license is converted into a mining lease. When financing for the Al Masane project is completed, the Company plans to make an application for an expanded exploration license for an area of approximately 2,800 square kilometers which includes the original Greater Al Masane area and the Wadi Qatan and Jebel Harr areas.

In May 1993, the Company had discussions with Chevron Chemical Company regarding the Company's proposal to purchase 5,000 barrels per day of mixed pentanes from an Aromax(R) petrochemical project to be built in Jubail, Saudi Arabia by Chevron Chemical in a joint venture with Saudi Venture Capital Group (SVCS). The Company and some Saudi partners, all of whom are directors and/or stockholders of the Company, plan to form a Saudi limited liability company which will build and manage a processing plant located next to the Aromax(R) plant in Saudi Arabia. The Company would have a 25% interest in the limited liability company and would manage the plant. The plant will be similar to the South Hampton refinery in producing purified pentanes from a feedstock of mixed pentanes obtained from the Aromax(R) plant. Chevron Chemical advised the Company by letter in July 1993 that Chevron Chemical and SVCS jointly agreed to commit to supply the proposed pentane project with up to 5,000 barrels per day of mixed pentane feedstock. Engineering and marketing studies of the project made in 1994 by outside consultants reflected positive results. Planning then began toward the construction and operation of the Aromax(R) plant and the processing plant. The Aromax(R) plant received final approval from the Saudi Arabian government in March 1996 and Chevron Chemical began construction soon thereafter. The source of feedstock supply to the Aromax(R) plant has changed resulting in Chevron

Chemical and SVCS being unable to supply the proposed processing plant. The Company has held discussions with several Saudi Arabian companies regarding feedstock and transportation arrangements, although there can be no assurances that any such arrangements can be made. The Company applied for and received a license to build the proposed processing plant and further planning and design work are underway.

In December 1993, the Company commissioned Sherritt Ltd. of Fort Saskatchewan, Canada, to prepare a conceptual engineering design for a proposed zinc refinery based on Sherritt's two stage pressure leach process, to be built by the Company and Saudi partners at the Red Sea port of Yanbu, Saudi Arabia. The refinery would have the capacity to produce 100,000 tonnes of slab zinc per year, with elemental sulfur as a by-product. Sherritt Ltd. completed the study in May 1994 which contains a proposed flow sheet

6

that has been commercialized and designed for a state of the art zinc refinery. Sherritt's zinc pressure leach technology provides significant advantages over other existing zinc production processes, including having the reputation as the most favored technology for environmental considerations. In its study, Sherritt concluded, after considering all of the presently identifiable elements, that they offer a strong potential for the project and enhance the concept. Sherritt encouraged the Company to carry out further studies toward the implementation of the project. There has been a recent inquiry about this project from a zinc smelting and refining company in Asia.

UNITED STATES ACTIVITIES. The Company's United States operations include the ownership and operation of a special products refinery and the leasing of mineral properties.

An indirect wholly owned subsidiary of the Company owns and operates a special products refinery near Silsbee, Texas which sells its products primarily to companies in the chemical and plastics industry. The refinery is presently devoted to specialized processing activities. Another indirect wholly owned subsidiary owns and operates three pipelines connected to the refinery.

The Company owns all of the capital stock of a coal company which does not presently own or hold any mineral interests and is presently inactive. The coal company had a net operating loss carryforward of approximately \$5.9 million at December 31, 1997.

The Company beneficially owns approximately 52% and directly owns approximately 44% of the outstanding capital stock of a company which leases mineral properties containing 129 inactive mining claims totalling approximately 3,600 acres in southeastern Nevada. There are prospects and mines on these claims which formerly produced silver, gold, lead, zinc and copper. In October 1997, Pioche entered into an Exploration Agreement and Option to Purchase with a large mining company which provides for annual payments to Pioche of \$50,000 for seven years until, or unless, the mining company exercises an option to purchase an 85% interest in the mining claims for \$3 million. The agreement can be terminated upon 60 days written notice by the mining company. The mining company has agreed to expend at least \$50,000 in exploration work each year and to drill at least one hole in the first year.

The Company leases office space in Jeddah, Saudi Arabia and in Dallas, Texas. It also has a base camp with a capacity to accommodate 60 people in its Al Masane mining lease area. The Company owns heavy mining equipment at the lease area, which will be used for future mining operations. The Company also has an exploration and drilling camp in the Wadi Qatan area in Saudi Arabia.

MARKET FOR THE COMPANY'S COMMON STOCK AND RELATED STOCKHOLDER MATTERS.

The Company's Common Stock traded on The NASDAQ Stock Market under the symbol: ARSD. The following table sets forth the high and low closing sale prices for each quarter of 1997 and 1996, respectively, as reported by NASDAQ.

<TABLE>
<CAPTION>

	1997				1996			
	1st	2nd	3rd	4th	1st	2nd	3rd	4th
<S>	<C> <C>	<C>	<C> <C>					
High	2 3/4	2	6 3/8	3 31/32	3 3/4	3 3/8	2 5/8	2 3/32
Low	1 1/2	1	1	1 3/4	1/4	1 1/2	1 1/2	1 5/8

At March 16, 1998, there were 831 record holders of the Company's Common Stock. The Company has not paid a dividend since its inception.

7

SELECTED FINANCIAL DATA.

The following is a five-year summary of selected financial data of the Company (in thousands, except per share amounts):

<TABLE>
<CAPTION>

	1997	1996	1995	1994	1993
<S>	<C>	<C>	<C>	<C>	<C>
Revenues.....	\$26,174	\$22,014	\$18,359	\$17,765	\$15,267
Net Income (Loss).....	\$ 818	\$ (391)	\$ (369)	\$ 2,852	\$ (1,338)
Net Income (Loss) Per Share.....	\$.04	\$ (.02)	\$ (.02)	\$.14	\$ (.08)
Total Assets (at December 31).....	\$45,053	\$44,096	\$40,805	\$41,057	\$41,090
Notes Payable (at December 31).....	\$11,376	\$11,376	\$15,086	\$15,945	\$18,044
Total Long-Term Obligations (at December 31).....	\$ 4,236	\$ 4,293	\$ 1,676	\$ 1,148	\$ 908

</TABLE>

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

The Company's revenues and cash flows have been insufficient to meet its debt service and capital expenditure requirements. Accordingly, it has been necessary for the Company continually to seek additional debt and equity financing in order to have funds to continue development and other investing activities. The Company experienced serious difficulties during prior years in obtaining additional financing, and is currently in need of additional funds to meet its obligations and continue development activities. The Company is exploring various alternatives for obtaining additional operating funds, including additional debt or equity financing, but there is no assurance that sufficient funds can be obtained. It is also possible that the terms of any additional financing that the Company is able to obtain will be unfavorable to the Company and its existing stockholders. For example, additional equity financing could result in a significant dilution of the interests of existing stockholders. Management of the Company expects to be devoting a significant amount of its attention in the near future to addressing the Company's immediate and longer term needs for the funds that are required in order to continue its business and maintain and develop its assets.

During 1997, the Company took certain actions designed to generate additional equity capital and improve its financial condition, including: (i) approval by the Company's Board of Directors in August 1997 of the sale of up to 1 million shares of the Company's Common Stock through private placements at a price no less than \$1.00 per share; (ii) the sale of 450,000 shares of the Company's Common Stock at \$1.00 per share to a Saudi Arabian investor who is a stockholder of the Company; (iii) the sale of 50,000 shares of the Company's Common Stock at \$1.00 per share to a Saudi Arabian investor; (iv) the issuance of 10,000 shares of its Common Stock at \$1.375 per share pursuant to an option exercise by an officer of the Company; (v) the issuance of 345,000 shares of its Common Stock in exchange for the cancellation of certain indebtedness; (vi) borrowing \$200,000 from a Saudi Arabian investor pursuant to a two-year demand promissory note bearing interest at prime plus 2% per annum; (vii) the sale by South Hampton Refining Company, an indirect, wholly owned subsidiary of the Company ("South Hampton"), in June 1997 of an office building to a third party for approximately \$695,000, on terms which included a ten-year promissory note having a principal amount of \$610,000 and bearing interest at 9% per annum; and (viii) receiving conditional approval for a \$38.08 million loan from the SIDF.

The exploration licenses held by the Company for the Wadi Qatan and Jebel Harr areas in Saudi Arabia, by their terms, have expired, although officials of the Saudi Arabian government have provided verbal assurance to the Company that the licenses will be extended as long as exploratory work is being carried out on the areas which they cover. None of the related projects at Al Masane or the other interests in Saudi Arabia were being developed at December 31, 1997 and significant additional expenditures will be necessary before commercial operations are commenced. A substantial portion of the Company's total assets is comprised of the mineral acquisition, exploration and development costs in Saudi Arabia. The ultimate recoverability of these deferred costs cannot be determined at the present time. The Company holds the mining lease for the Al Masane area exclusively.

8

The 1996 update to the 1994 feasibility study shows the estimated total capital cost to bring the Al Masane project into production to be \$88.6 million. At the present time, the Company does not have sufficient funds to bring the project into production.

On May 20, 1996, the Company entered into a Financial and Legal Services and Advice Agreement with Nasir Ali Kadasah, for legal advice, and Dar Al Khaleej, a Saudi Arabian consulting company, for research and economic advice. The purpose of this agreement was for the two Saudi Arabian advisors to assist the Company in obtaining financing for the Al Masane project. To this end, the agreement contemplated that the Saudi Arabian advisors would perform the following:

1. The formation of a Saudi limited liability company, 50% of which would be owned by the Company and the remaining 50% of which would be owned by Saudi Arabian investors who will contribute 25% of the total capital cost of the project.
2. Obtain an industrial license for the project from the Ministry of Industry and Electricity. This license was a necessary prerequisite for

obtaining an interest-free loan from the Saudi Industrial Development Fund ("SIDF") to fund 50% of the capital cost of the project.

3. Finalize the necessary procedures to obtain such loan from the SIDF, the application for which was submitted on September 30, 1995.

4. Apply for and receive loans from commercial banks necessary to finance the project.

5. Apply for and obtain the Ministerial Resolution from the Minister of Petroleum and Mineral Resources approving the transfer of the mining lease to the Saudi limited liability company.

The agreement provided that the Saudi Arabian advisors would be solely responsible for the performance of the foregoing obligations and that the Company had no obligation therefor.

As consideration for performing these obligations, the Company agreed to pay Mr. Kadasah and Dar Al Khaleej \$10,000 each upon the issuance of the industrial license and Mr. Kadasah \$10,000 upon approval of the loan by the SIDF. The Company also agreed to issue to Mr. Kadasah and Mr. Tawfiq Abdulaziz Al-Sowailim, as agent for Dar Al Khaleej, up to 1,025,000 and 975,000 shares of the Company's Common Stock, respectively, and to grant Mr. Kadasah and Mr. Tawfiq Abdulaziz Al-Sowailim, as agent for Dar Al Khaleej, options to purchase up to 1,425,000 and 875,000 shares of the Company's Common Stock, respectively. The Company was obligated to issue such shares and grant such options in designated amounts upon completion of each of the foregoing obligations. The issuance of the shares would be for consideration consisting solely of services rendered to the Company. The options are immediately exercisable on the date of grant, have a five-year term commencing on the date of formation of the Saudi limited liability company and an exercise price of \$1.00 per share. On December 3, 1996, the industrial license was issued to the Company and its Saudi Arabian advisors. As a result, the Company paid the advisors \$20,000 in the aggregate and was obligated at December 31, 1997 to issue to these advisors 300,000 shares of the Company's Common Stock in the aggregate and options to purchase 345,000 shares of the Company's Common Stock in the aggregate having an exercise price of \$1.00 per share. The agreement was terminated in August 1997 and negotiations are being held to complete a new agreement, although there can be no assurances that any such agreement can be reached.

A loan application was submitted to SIDF on September 30, 1995 and conditional approval was received on December 17, 1997 for a \$38.08 million loan. The SIDF makes interest-free loans to industrial projects in Saudi Arabia and charges a 2.5% service fee. The Company believes that it may also be able to finance the remaining cost of the project through arrangements with suppliers and equipment manufacturers, custom smelters and additional debt or equity financing secured by the Company, however, there can be no assurances to that effect.

On November 5, 1997, the Company initialed a joint venture agreement with Al Mashreq Company for Mining Investments ("Al Mashreq"), a Saudi limited liability company owned by Saudi Arabian investors,

9

which contemplates the formation of a new Saudi limited liability company, "The Arabian Shield Company for Mining Industries Ltd.", to be owned 50% by the Company and 50% by Al Mashreq. As contemplated, the Saudi limited liability company will be responsible for the construction and operation of the mining facilities. Title to the mining lease would be transferred to the Saudi limited liability company. The joint venture agreement further contemplates the Company transferring its beneficial interest in the Al Masane project to the Saudi limited liability company when title to the mining lease is transferred to the Saudi limited liability company. The Company and Al Mashreq agree to attempt to obtain financing for the project, and that if firm commitments for such financing on acceptable terms are not obtained by November 5, 1998, either party may terminate the agreement without liability, except that the Company will return to Al Mashreq any consideration paid for the assignment of the beneficial interest in the project and full title to the mining lease will revert to the Company.

Pursuant to the mining lease agreement, when the profitability of the project is established, the Company is obligated to form a Saudi public stock company with Petromin. It is contemplated that the Saudi limited liability company then will be transformed into a Saudi public stock company, that the Company and Al Mashreq will own no less than 50% of the shares of the Saudi public stock company, that Petromin will have an option to acquire up to 25% of the shares and that the remaining shares will be offered for sale in Saudi Arabia pursuant to a public subscription. Title to the mining lease and the other obligations specified in the mining lease will be transferred to the Saudi public stock company. Responsibility for the repayment of the \$11 million loan from the Saudi Arabian government will remain with the Company. In December 1994, the Company received instructions from the office of the Minister of Petroleum and Mineral Resources stating that it is possible for the Company to form a Saudi company without Petromin but that the sale of stock to the Saudi public could occur only after two years of profits from commercial operations of the mine. The instructions added that Petromin will still have the right to purchase shares in the Saudi public stock company any time it desires.

On October 15, 1996, South Hampton entered into an Amended and Restated Credit Agreement (the "Credit Agreement") with Den norske Bank ASA (the "Bank"), amending and restating the then outstanding credit agreement to provide for a revolving loan facility in an aggregate principal amount of up to \$1,965,000. The Bank's commitment to make funds available under the credit facility will be reduced by (i) \$75,000 on the last day of each fiscal quarter commencing December 31, 1996 and (ii) the amount of any distribution by South Hampton to Saudi Fal Co., Ltd. ("Saudi Fal"), the Company, American Shield Refining Company, a wholly owned subsidiary of the Company (the "Refining Company"), or Texas Oil and Chemical Co. II, a wholly owned subsidiary of the Refining Company ("TOCCO"), in excess of amounts permitted under the Credit Agreement. Advances under the Credit Agreement may not at any time exceed the lesser of the commitment or a borrowing base calculated based upon the cash collateral account, eligible accounts receivable and inventory. Interest is payable monthly in arrears on all outstanding advances under the credit facility at the Bank's prime lending rate, as in effect from time to time, plus 1%. Principal and accrued and unpaid interest was payable on December 31, 1998, but in March 1998 the maturity date was extended to December 31, 1999. Subject to certain conditions and South Hampton maintaining various financial covenants and ratios, the Credit Agreement permits South Hampton to make distributions to (i) Saudi Fal, the Company, the Refining Company and TOCCO for legal, auditing and accounting fees attributable to the operations of South Hampton in an annual aggregate amount not in excess of \$60,000, (ii) Saudi Fal and the Company in respect of accrued interest on any debt owned by South Hampton to Saudi Fal or the Company in an amount not in excess of \$17,500 per month and (iii) Saudi Fal and the Company in respect of principal on any debt owed by South Hampton to Saudi Fal or the Company. The Credit Agreement is secured by all of the assets of South Hampton and Gulf State Pipe Line Company, Inc., a wholly owned subsidiary of South Hampton ("Gulf State"), and all of the issued and outstanding shares of TOCCO, South Hampton and Gulf State. South Hampton is required to collect all receivables through a cash collateral account at a local bank.

In connection with South Hampton's entry into the Credit Agreement with the Bank, South Hampton issued a Second Lien Promissory Note to Saudi Fal and a Third Lien Promissory Note to the Refining

10

Company in the original principal amounts of \$1,945,773.49 and \$1,694,605.08, respectively, evidencing certain indebtedness of South Hampton owed to such parties. The promissory notes bear interest at the Bank's prime lending rate, as in effect from time to time, plus 1%. Interest only is due and payable monthly on the promissory notes, and the entire unpaid balance of principal and accrued and unpaid interest was due on December 31, 1998, but in March 1998 the maturity date was extended to December 31, 1999. The promissory notes are secured by all of the assets of South Hampton and Gulf State. The promissory notes and related liens are subordinated to the Credit Agreement. The promissory note issued to the Refining Company and related liens are subordinate to the promissory note issued to Saudi Fal.

The Clean Air Act Amendments of 1990 have had a positive effect on the refinery's business as plastics manufacturers are searching for ways to use more environmentally acceptable solvents in their processes. Plastics manufacturers have historically used C6 hydrocarbons (hexanes) as coolants and catalyst carrying agents. There is a current trend among plastics manufacturers toward the use of lighter and more recoverable C5 hydrocarbons (pentanes) which are a large part of the refinery's product line. Management believes that the refinery's ability to manufacture high quality solvents in the C5 hydrocarbon market will provide the basis for growth over the next few years; however, there can be no assurance that such growth will occur. While the refinery continues to manufacture C6 solvents, its manufacturing of these solvents is being phased out. The Aromax(R) unit, which was jointly developed by the refinery and Chevron Research, has the ability to convert C6 hydrocarbons into benzene and other more valuable aromatic compounds, which was part of the reason the refinery participated in the Aromax(R) development project initially.

The Company's financial statements have been prepared assuming that the Company will continue as a going concern. The Company's current primary source of cash flow is attributable to the refinery which is fully dedicated to the repayment of debt and the funding of refinery operations. The Company is not presently generating any cash flow from any of its other activities. Management plans to fund future operations initially through sales of its Common Stock and borrowings. It is expected that the operations and obligations of the Company will be eventually funded from operations of the Al Masane mine. However, because of uncertainties with respect to future sales of Common Stock, obtaining suitable financing and reaching an agreement on the repayment of the loan to the Saudi Arabian government, there is substantial doubt about the Company's ability to continue as a going concern. The Company's financial statements do not include any adjustments that might result from the outcome of these uncertainties.

RESULTS OF OPERATIONS

COMPARISON OF THE YEARS 1997 TO 1996

During the fiscal year ended December 31, 1997, the Company had a net income of \$818,364 compared to a net loss of \$390,896 for the fiscal year ended December

31, 1996.

The gross revenues in 1997 of \$26,174,119 was an increase of \$4,159,833 from 1996 while the cost of sales in 1997 of \$22,119,668 was an increase of \$2,761,931 from 1996, resulting in a net margin increase in 1997 of \$1,462,231. After processing fee income, general and administrative expenses and depreciation and amortization, the operating income of the Company in 1997 of \$821,168 was an improvement of \$1,142,292 over the operating loss in 1996 of \$321,124. The net income for the refinery in 1997 of \$1,171,206 was \$1,036,815 more than the net income in 1996 of \$134,391.

The refinery's net income for 1997 increased despite operating losses during the first two months of the year resulting from the increased prices of natural gasoline, its primary feedstock, and natural gas used for fuel. During March 1997, feedstock prices and natural gas fuel prices returned to their normal levels which, combined with an increase in the sales prices of the refinery's products, resulted in improved gross and operating margins. The volume of refined products sold increased 14% to 28 million gallons versus 24.5 million gallons sold in 1996. The total volume of refined product sales was the largest volume achieved by the refinery since it began processing special products in 1985. The strong volume of sales

11

reflected increased sales to existing customers and an increased marketing effort which resulted in new customers. The plastics industry continued to experience a steady demand which resulted in the continued growth in the volume of refined products sold.

The primary feedstock of the refinery, natural gasoline, is the heavier liquid produced by natural gas processing plants and by LPG fractionators. Feedstock prices in 1997 were on average identical to 1996 prices. The refinery's products had an average selling price approximately 4% above 1996 levels, resulting in gross margins for the year being slightly above the 1996 average gross margin. The chemical industry, particularly the ethylene crackers, continued to be the big user of natural gasoline in 1997 which contributed to feedstock prices remaining higher than in recent years. Feedstock prices, which peaked during the period from November 1996 through February of 1997, returned to their former levels throughout most of 1997 and decreased in the fourth quarter of 1997.

With the exception of 1997 when toll processing fees decreased as a result of the cancellation of a processing contract, the refinery has experienced a healthy growth in its toll processing business over the last several years. Toll processing and tank rental fees were \$694,797, \$724,849 and \$660,519 in 1995, 1996 and 1997, respectively. The increase in the toll processing business is indicative of the direction of the refining and petrochemical industries in the U.S. Many larger companies are "right sizing" and outsourcing smaller jobs and processes which have been formerly managed within their own facilities. The refinery has been in the toll processing business for over 30 years and enjoys a good reputation in the industry. Management intends to expand the refinery's involvement in this area as opportunities arise.

General and administrative expenses increased by \$410,621, or 18%, to \$2,695,043 in 1997 from \$2,284,422 in 1996. A portion of this increase was attributable to stock option expenses of \$125,000 and \$50,000 for the cost of issuing 50,000 shares at no cost in 1997. Interest expense, which was practically all attributable to the debt of the refinery, increased by \$68,291 from \$336,979 in 1996 to \$405,270 in 1997. This increase was primarily due to an increased amount of interest bearing debt, which was a result of a major debt restructuring in October 1996 when accrued interest was rolled over into principal and the new interest rates were higher.

There has been no activity in several years on the Pioche Ely Valley Mines, Inc. ("Pioche") properties primarily due to the lack of financing for claims to be explored and developed; however, in October 1997, Pioche entered into an Exploration Agreement and Option to Purchase with a large mining company. Interest income in 1997 and 1996 was from the investment of temporary excess cash in time deposits in Saudi Arabia and a short-term investment by the refinery. In 1997 and 1996, there was no operating activity on any of the Saudi Arabia mining properties. Assuming financing can be obtained, the results of the 1996 update to the 1994 feasibility study contemplate that construction of an ore treatment plant and all infrastructure for a mining facility at Al Masane is estimated to take 18 months to complete at an estimated cost of \$88.6 million, an increase of \$7.3 million over the 1994 study estimate.

Miscellaneous income represents various items of other income which individually are not significant enough to warrant being separately disclosed. These items primarily include income from tank rentals, building rentals, commission income and occasional small asset sale proceeds. In 1997 and 1996, the refinery received \$25,410 and \$101,640, respectively, from the leasing of an office building. This office building was sold to the lessee in June 1997. Tank rentals accounted for \$78,000 in each year.

Primarily as a result of the Company's write-off of its total investment in the coal leases in 1988, the Company had net operating loss carryforwards of approximately \$32.3 million at December 31, 1997, of which approximately \$5.9 million is limited to any future net income of the coal company and approximately \$1.7 million is limited to any future net income of the refinery. These carryforwards expire during the years 1998 through 2011.

At December 31, 1997, a total of approximately \$1,581,000 in salaries and termination benefits accrued since 1971 was due to Company employees in Saudi Arabia in accordance with Saudi Arabian employment laws, which includes approximately \$779,000 due to Hatem El-Khalidi, the Company's President and Chief Executive Officer. Accrued salaries and termination benefits to Company employees

12

in Saudi Arabia and to Mr. El-Khalidi at December 31, 1996 were approximately \$776,000 and \$714,000, respectively. The payment of these amounts has been deferred until the Company's working capital position improves.

COMPARISON OF THE YEARS 1996 TO 1995

During the fiscal year ended December 31, 1996, the Company had a net loss of \$390,896 compared to a net loss of \$369,232 for the fiscal year ended December 31, 1995.

The gross refined product sales in 1996 of \$21,367,438 was an increase of \$3,625,576 from 1995 while the cost of sales in 1996 of \$19,357,737 was an increase of \$3,782,683 from 1995, resulting in a net margin decrease in 1996 of \$157,107. After processing fee income, general and administrative expenses and depreciation and amortization, the operating loss of the Company in 1996 of \$321,124 was \$54,888 more than the operating loss in 1995 of \$266,236. The net income for the refinery in 1996 of \$134,391 was \$225,210 less than the net income in 1995 of \$359,601.

The refinery's net income in 1996 was not indicative of its performance for the year. The volume of refined products sold increased 18% to 24.5 million gallons versus 20.8 million gallons sold in 1995. The strong volume of sales reflected increased sales to existing customers and an increased marketing effort which resulted in new customers. The plastics industry continued to experience a steady demand which resulted in the continued growth in the volume of refined products sold. However for much of 1996 and particularly in the last two months of the year, gross and operating margins were weaker than the refinery had experienced in recent years. During the fourth quarter and particularly in November and December of 1996, feedstock prices and natural gas fuel prices increased to unusual high levels eroding the refinery's steady performance over the first ten months of the year. Sales commitments and competitive pressures did not allow the refinery to pass through the higher costs immediately, although by the first quarter of 1997 selling prices had been raised. The refinery's focus on producing products in the higher priced solvents markets allowed it to raise selling prices during the year although not enough to offset the total spike in feed costs at year end.

The primary feedstock of the refinery, natural gasoline, is the heavier liquid produced by natural gas processing plants and by LPG fractionators. Feedstock prices in 1996 were 10% higher than in 1995 resulting in reduced gross margins on sales. The chemical industry, particularly the ethylene crackers, continued to be the big user of natural gasoline in 1996 which contributed to the higher feedstock prices. Feedstock prices, which peaked during the period from November 1996 through February of 1997, have returned to their former levels and are expected to remain there for most of 1997.

The refinery has experienced a healthy growth in its toll processing business over the last three years and expects the opportunities to continue to develop, although there can be no assurances to that effect. Toll processing and tank rental fees were \$297,757, \$694,797 and \$724,849 in 1994, 1995 and 1996, respectively. The increase in the toll processing business is indicative of the direction of the refining and petrochemical industries in the U.S. Many larger companies are "right sizing" and outsourcing smaller jobs and processes which have been formerly managed within their own facilities. The refinery has been in the toll processing business for over 30 years and has a good reputation in the industry for this type of work. Management intends to expand the refinery's involvement in this area as opportunities arise.

General and administrative expenses decreased by \$88,261 to \$2,284,422 in 1996 from \$2,372,683 in 1995. This decrease was mostly attributable to a stock option expenses of \$151,431 in 1995. Interest expense, which was practically all attributable to the debt of the refinery, decreased slightly by \$32,567 from \$369,546 in 1995 to \$336,979 in 1996. This decrease was primarily due to a reduced amount of debt at the refinery in 1996.

The equity in losses of affiliate in 1995 and 1994 was attributable to the cost of maintaining the Nevada mining properties of Pioche Ely Valley Mines, Inc. ("Pioche"). In 1996, the Company concluded that its voting control of Pioche was no longer temporary and, therefore, the asset and liability amounts of Pioche have been consolidated into its financial statements. The minority interest in 1996 of \$13,072 represents

13

the Pioche minority shareholders portion of Pioche's 1996 loss. There has been no activity in several years on the Pioche properties primarily due to the lack of financing for claims to be explored and developed. Interest income in 1996 and 1995 was from the investment of temporary excess cash in time deposits in

Saudi Arabia and a short-term investment by the refinery. In 1996 and 1995, there was no operating activity on any of the Saudi Arabia mining properties. Assuming financing can be obtained, the results of the 1996 update to the 1994 feasibility study contemplate that construction of an ore treatment plant and all infrastructure for a mining facility at Al Masane is estimated to take 18 months to complete at an estimated cost of \$88.6 million, an increase of \$7.3 million over the 1994 study estimate.

Miscellaneous income represents various items of other income which individually are not significant enough to warrant being separately disclosed. These items primarily include income from tank rentals, building rentals, commission income and occasional small asset sale proceeds. In 1996 and 1995, the refinery received \$101,640 each year from the leasing of an office building. Tank rentals accounted for \$78,000 in each year.

Primarily as a result of the Company's write-off of its total investment in the coal leases in 1988, the Company had net operating loss carryforwards of approximately \$33.3 million at December 31, 1996, of which approximately \$5.9 million is limited to any future net income of the coal company and approximately \$1.7 million is limited to any future net income of the refinery. These carryforwards expire during the years 1997 through 2010.

At December 31, 1996, a total of approximately \$1,490,000 in salaries and termination benefits accrued since 1971 was due to Company employees in Saudi Arabia in accordance with Saudi Arabian employment laws, which includes approximately \$714,000 due to Hatem El-Khalidi, the Company's President and Chief Executive Officer. Accrued salaries and termination benefits to Company employees in Saudi Arabia and to Mr. El-Khalidi at December 31, 1995 were approximately \$1,373,000 and \$636,000, respectively. The payment of these amounts has been deferred until the Company's working capital position improves.

OTHER MATTERS

Year 2000. The Year 2000 issue relates to computer systems and applications that currently use two-digit date fields to designate a year. As the century date change occurs, date-sensitive systems will recognize the Year 2000 as 1900, or not at all. This inability to recognize or properly treat the Year 2000 may cause systems to process critical financial and operational information incorrectly, which may have a material adverse effect on the Company's business, operating results and financial condition.

The Company is utilizing both internal and external resources to identify, correct or reprogram and test information systems for Year 2000 compliance. The Company estimates that its costs for addressing the Year 2000 issue will be approximately \$25,000. These costs will be expensed as incurred.

Furthermore, there can be no assurance that the Company's customers and suppliers are or will be Year 2000 compliant. The failure of the Company's customers and suppliers to achieve Year 2000 compliance could have a material adverse effect on the Company's business, operating results and financial condition.

Quantitative and Qualitative Disclosures About Market Risks. The market risk inherent in the Company's financial instruments represents the potential loss resulting from adverse changes in interest rates, foreign currency rates and commodity prices. The Company's exposure to interest rate changes results from its variable rate debt instruments which are vulnerable to changes in short term United States prime interest rates. At December 31, 1997, the Company had \$4.0 million in variable rate debt outstanding. A hypothetical 10% change in interest rates underlying these borrowings would result in approximately a \$38,000 annual change in the Company's earnings and cash flows.

14

The Company is exposed to market risk in the exchange rate of the Saudi Arabian riyal as measured against the United States dollar. The Company does not view this exposure as significant and has not acquired or issued any foreign currency derivative financial instruments. The Company's strategy in managing its exposure to commodity prices is to purchase options on commodity based derivative futures contracts. At December 31, 1997, the Company's investment in such instruments was insignificant.

15

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REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

Board of Directors and Stockholders
Arabian Shield Development Company

We have audited the accompanying consolidated balance sheets of Arabian Shield Development Company and Subsidiaries as of December 31, 1997 and 1996 and the related consolidated statements of operations, stockholders' equity, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit 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 consolidated financial position of Arabian Shield Development Company and Subsidiaries as of December 31, 1997 and 1996, and the consolidated results of their operations and their consolidated cash flows for the years then ended, in conformity with generally accepted accounting principles.

The accompanying financial statements have been prepared assuming the Company will continue as a going concern. As discussed in Note 2 to the financial statements, the Company's sources of cash flow in 1997 were the operations of its refinery and the proceeds from loans and the sale of common stock. Cash flow from the refinery is dedicated to repaying debt and funding refinery operations. As discussed in Notes 5 and 7 to the financial statements, the majority of the Company's assets consist of costs related to the acquisition, exploration, and development of mineral interests in Saudi Arabia. The ability of the Company to develop these properties is dependent upon obtaining additional financing. As discussed in Note 9, the Company is obligated to the Saudi Arabian government for a loan in the amount of \$11,000,000. The Company does not currently have the financial resources to pay this obligation and is attempting to reschedule the payment. Management's plans with regard to these matters are discussed in Note 2. These matters raise substantial doubt about the Company's ability to continue as a going concern. The financial statements do not include any adjustments that might result from the outcome of these uncertainties .

As discussed in Note 3, the Company adopted the consolidation method of accounting for its investment in Pioche-Ely Valley Mines, Inc. in 1996.

GRANT THORNTON LLP

Dallas, Texas
March 13, 1998

16

REPORT OF INDEPENDENT ACCOUNTANTS

To The Stockholders and Board of Directors
of Arabian Shield Development Company

In our opinion, the accompanying consolidated statements of operations, of stockholders' equity and of cash flows present fairly, in all material respects, the results of operations and cash flows of Arabian Shield Development Company and its subsidiaries for the year ended December 31, 1995, in conformity with generally accepted accounting principles. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit of these statements in accordance with generally accepted auditing standards which require that we plan and perform the audit 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, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for the opinion expressed above. We have not audited the consolidated financial statements of Arabian Shield Development Company for any period subsequent to December 31, 1995.

The accompanying consolidated financial statements have been prepared assuming that the Company will continue as a going concern. As described in Note 2 to the financial statements, the Company's primary source of cash flow is fully dedicated to repayment of debt and funding of refinery operations. Additionally, the Company is not generating cash flow from any of its other activities. These matters raise substantial doubt about its ability to continue as a going concern. Management's plans in regard to these matters are described in Note 2. The financial statements do not include any adjustments that might result from the outcome of these uncertainties.

As described in Notes 5 and 7 to the financial statements, a substantial portion of the Company's total assets is comprised of mineral acquisition, exploration and development costs relating to its interests in Saudi Arabia which have been deferred at December 31, 1995. None of the related projects have been developed for commercial operation as of December 31, 1995, and significant expenditures, for which the Company must obtain financing, will be necessary before commercial operations, if any, are commenced.

As described in Note 9 to the financial statements, the Company is in default on repayment of an \$11 million loan from the Saudi Arabian government which was made to the Al Masane Project. The Company is attempting to reschedule payment of the loan.

As described in Note 9 to the financial statements, the Company's refining subsidiary, South Hampton Refining Company ("South Hampton"), has short-term notes payable and current portions of long-term obligations totaling \$3.8 million. South Hampton does not have the ability to fully repay these current obligations from internally generated funds. Arabian Shield Development Company has not guaranteed the debt obligations of South Hampton. The Company's financial statements do not include any adjustments that might be necessary should South Hampton be unable to satisfy its current obligations in an orderly manner.

PRICE WATERHOUSE LLP

Dallas, Texas
March 25, 1996

17

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

ASSETS

<TABLE>
<CAPTION>

	DECEMBER 31,	
	1997	1996
<S>	<C>	<C>
Current Assets		
Cash and cash equivalents.....	\$ 534,086	\$ 385,290
Short-term investments.....	407,542	298,726
Trade receivables.....	3,047,311	2,643,691
Inventories.....	548,320	565,346
Total current assets.....	4,537,259	3,893,053
Refinery Plant, Pipeline and Equipment -- At Cost.....	5,926,188	5,758,852
Less Accumulated Depreciation.....	(3,238,623)	(2,911,823)
Refinery Plant, Pipeline and Equipment, Net.....	2,687,565	2,847,029
Al Masane Project.....	33,522,427	32,882,838
Other Interests in Saudi Arabia.....	2,431,248	2,431,248
Mineral Properties in the United States.....	1,411,190	1,418,615
Goodwill.....	--	117,598
Other Assets.....	463,230	505,566
Total Assets.....	\$45,052,919	\$44,095,947

</TABLE>

18

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS -- CONTINUED

LIABILITIES AND STOCKHOLDERS' EQUITY

<TABLE>
<CAPTION>

	DECEMBER 31,	
	1997	1996
<S>	<C>	<C>
Current Liabilities		
Accounts payable-trade.....	\$ 790,759	\$ 1,408,677
Accrued liabilities.....	673,511	520,445
Accrued liabilities in Saudi Arabia.....	1,283,401	1,174,229
Notes payable.....	11,375,780	11,375,780
Current portion of long-term debt.....	598,000	992,729
Current portion of long-term obligations.....	37,915	150,904
Total current liabilities.....	14,759,366	15,622,764
Long-Term Debt.....	3,435,773	3,544,112
Long-Term Obligations.....	21,205	35,009
Accrued Liabilities in Saudi Arabia.....	779,149	714,143
Deferred Revenue.....	114,181	129,685
Commitments and Contingencies.....	--	--
Minority Interest in Consolidated Subsidiary.....	1,044,487	1,003,590
Stockholders' Equity		
Common stock, authorized 40,000,000 shares of \$.10 par value: issued and outstanding, 21,861,494 shares in		

1997 and 20,956,494 shares in 1996.....	2,186,149	2,095,649
Additional paid-in capital.....	35,875,950	34,932,700
Receivable from stockholder.....	(126,000)	(126,000)
Accumulated deficit.....	(13,037,341)	(13,855,705)
	-----	-----
Total stockholders' equity.....	24,898,758	23,046,644
	-----	-----
Total Liabilities and Stockholders' Equity.....	\$45,052,919	\$44,095,947
	=====	=====

</TABLE>

The accompanying notes are an integral part of these statements.

19

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS
FOR THE THREE YEARS ENDED DECEMBER 31, 1997

<TABLE>
<CAPTION>

	1997	1996	1995
	-----	-----	-----
<S>	<C>	<C>	<C>
Revenues			
Refined product sales.....	\$25,591,600	\$21,367,438	\$17,741,862
Processing fees.....	582,519	646,848	616,796
	-----	-----	-----
	26,174,119	22,014,286	18,358,658
Operating costs and expenses			
Cost of refined product sales and processing.....	22,119,668	19,357,737	15,575,054
General and administrative.....	2,695,043	2,284,422	2,372,683
Depreciation and amortization.....	538,240	693,251	677,157
	-----	-----	-----
	25,352,951	22,335,410	18,624,894
Operating income (loss).....	821,168	(321,124)	(266,236)
Other income (expense)			
Interest income.....	51,062	25,310	33,395
Interest expense.....	(405,270)	(336,979)	(369,546)
Minority interest.....	19,282	13,072	--
Equity in losses of affiliate.....	--	--	(24,112)
Miscellaneous income.....	332,122	228,825	257,267
	-----	-----	-----
Net income (loss).....	\$ 818,364	\$ (390,896)	\$ (369,232)
	=====	=====	=====
Net income (loss) per common share:			
Basic.....	\$ 0.04	\$ (0.02)	\$ (0.02)
	=====	=====	=====
Diluted.....	\$ 0.04	\$ (0.02)	\$ (0.02)
	=====	=====	=====
Weighted average number of common and common equivalent shares outstanding:			
Basic.....	21,306,040	20,286,208	20,030,434
	=====	=====	=====
Diluted.....	22,017,652	20,286,208	20,030,434
	=====	=====	=====

</TABLE>

The accompanying notes are an integral part of these statements.

20

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

<TABLE>
<CAPTION>

	COMMON STOCK		ADDITIONAL	RECEIVABLE	ACCUMULATED	TOTAL
	SHARES	AMOUNT	PAID-IN	FROM	DEFICIT	
	-----	-----	CAPITAL	STOCKHOLDER	-----	-----
<S>	<C>	<C>	<C>	<C>	<C>	<C>
December 31, 1994.....	20,028,494	\$2,002,849	\$32,899,119	\$ (276,000)	\$ (13,095,577)	\$21,530,391
Common stock and common stock subscriptions sold.....	278,000	27,800	250,200	--	--	278,000
Payment on stockholder receivables.....	--	--	--	50,000	--	50,000
Write-off of stockholder receivable.....	(100,000)	(10,000)	(90,000)	100,000	--	--
Stock options issued.....	--	--	151,431	--	--	151,431
Net loss.....	--	--	--	--	(369,232)	(369,232)
	-----	-----	-----	-----	-----	-----
December 31, 1995.....	20,206,494	2,020,649	33,210,750	(126,000)	(13,464,809)	21,640,590

Common stock sold.....	450,000	45,000	405,000	--	--	450,000
Common stock issued for services.....	300,000	30,000	520,000	--	--	550,000
Stock options issued.....	--	--	796,950	--	--	796,950
Net loss.....	--	--	--	--	(390,896)	(390,896)
December 31, 1996.....	20,956,494	2,095,649	34,932,700	(126,000)	(13,855,705)	23,046,644
Common stock sold.....	500,000	50,000	450,000	--	--	500,000
Common stock issued for services.....	50,000	5,000	45,000	--	--	50,000
Common stock issued on debt conversion.....	345,000	34,500	310,500	--	--	345,000
Stock options exercised.....	10,000	1,000	12,750	--	--	13,750
Stock options issued for services.....	--	--	125,000	--	--	125,000
Net income.....	--	--	--	--	818,364	818,364
December 31, 1997.....	21,861,494	\$2,186,149	\$35,875,950	\$(126,000)	\$(13,037,341)	\$24,898,758

</TABLE>

The accompanying notes are an integral part of these statements.

21

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE THREE YEARS ENDED DECEMBER 31, 1997

<TABLE>
<CAPTION>

	1997	1996	1995
	<C>	<C>	<C>
Operating activities			
Net income (loss).....	\$ 818,364	\$(390,896)	\$(369,232)
Adjustments for non-cash transactions			
Depreciation and amortization.....	538,240	693,251	677,157
Equity in losses of affiliate.....	--	--	24,112
Common stock and stock options issued for services.....	175,000	--	151,431
Effects of changes in			
Increase in trade receivables.....	(403,620)	(845,570)	(388,839)
Decrease (increase) in inventories.....	17,026	(134,614)	40,342
Decrease in other assets.....	42,336	135,287	87,016
(Decrease) increase in accounts payable and accrued liabilities.....	(464,852)	454,810	(267,830)
Decrease in deferred revenue.....	(15,504)	(15,504)	(15,504)
Other.....	(7,945)	(70,529)	(12,190)
Net cash provided by (used for) operating activities.....	699,045	(173,765)	(73,537)
Investing activities			
Additions to short-term investments.....	(108,816)	(4,116)	(291,915)
Proceeds from sale of short-term investments.....	--	--	255,787
Additions to Al Masane Project.....	(639,589)	(451,110)	(785,751)
Additions to refinery plant, pipeline and equipment.....	(167,336)	(195,076)	(153,235)
Reduction in mineral properties in the United States.....	7,425	--	--
Decrease in cash in Saudi Arabia.....	--	396,809	34,167
Increase in accrued liabilities in Saudi Arabia....	174,178	53,450	276,366
Net cash used for investing activities.....	(734,138)	(200,043)	(664,581)
Financing activities			
Common stock sold.....	513,750	450,000	--
Decrease in receivable from stockholder.....	--	--	50,000
Additions to notes payable and long-term obligations.....	200,000	445,773	721,000
Reduction of notes payable and long-term obligations.....	(529,861)	(438,714)	(809,192)
Net cash provided by (used for) financing activities.....	183,889	457,059	(38,192)
Net increase (decrease) in cash.....	148,796	83,251	(776,310)
Cash and cash equivalents at beginning of year.....	385,290	302,039	1,078,349
Cash and cash equivalents at end of year.....	\$ 534,086	\$ 385,290	\$ 302,039

</TABLE>

The accompanying notes are an integral part of these statements.

22

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 -- BUSINESS AND OPERATIONS OF THE COMPANY

Since its organization on May 4, 1967, the principal activity of Arabian Shield Development Company (the "Company") has been the exploration and development of mineral deposits in Saudi Arabia (Note 7). In February 1986, the Company purchased all of the issued and outstanding capital stock of Dorchester Coal Company, which was subsequently renamed American Shield Coal Company (the "Coal Company") and is currently dormant. The Company, through its wholly-owned subsidiary American Shield Refining Company (the "Refining Company"), owns all of the outstanding common stock of Texas Oil and Chemical Company II, Inc. ("TOCCO"). South Hampton Refining Company ("South Hampton") is a wholly-owned subsidiary of TOCCO, and Gulf State Pipe Line Company, Inc. ("Gulf State") is a wholly-owned subsidiary of South Hampton. The principal assets of TOCCO and its subsidiaries are a specialty products refinery located outside of Beaumont, Texas, which currently processes light naphtha feedstock, and 50 miles of natural gas and product pipelines which connect the refinery to supplies and a marine terminal on the Neches River near Beaumont. The Company also owns 44% of Pioche-Ely Valley Mines, Inc. ("Pioche") which owns mineral deposits in Nevada (Note 8). Pioche has been consolidated for financial statement purposes since January 1, 1996.

NOTE 2 -- GOING CONCERN

The accompanying consolidated financial statements have been prepared assuming the Company will continue as a going concern. The Company's sources of cash flow in 1997 were the operations of South Hampton's refinery and the proceeds from stock sales and loans. The Company is not currently generating cash flow from any other activities. As the cash flow attributable to South Hampton is fully dedicated to repayment of debt and funding of refinery operations (described in Note 9), the cash flow attributable to South Hampton currently is not adequate to support the Company's operations. As described in Note 9, the Company is liable to the Saudi Arabian government for an \$11,000,000 loan. The Company does not currently have the financial resources to pay this obligation.

Management plans to fund future operations initially through sales of its common stock and borrowings. It is expected that the operations and obligations of the Company will be eventually funded from operations of the Al Masane mine. However, because of uncertainties with respect to future sales of common stock, obtaining suitable financing, and reaching an agreement on the repayment of the loan to the Saudi Arabian government, there is substantial doubt about the Company's ability to continue as a going concern. These financial statements do not include any adjustments that might result from the outcome of these uncertainties.

NOTE 3 -- SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation -- The Company consolidates all subsidiaries for which it has majority ownership or voting control which is other than temporary. All material intercompany accounts and transactions are eliminated.

As discussed in Note 8, the Company owns 44% of Pioche and has had voting control for a number of years as a result of a loan which is collateralized by 8% of the outstanding common stock of Pioche. In 1996, the Company concluded that its voting control of Pioche was no longer temporary. Therefore, Pioche has been consolidated in 1996 and 1997. The financial statements for 1995, which account for the investment in Pioche on the equity method, have not been restated.

Cash and cash equivalents -- The Company considers all highly liquid investments with an original maturity of three months or less to be cash equivalents.

Short-term investment -- At December 31, 1997 and 1996, the Company held a United States treasury bill with an original maturity of less than one year. The Company intends to hold this investment to maturity.

Inventories -- Refined products and feedstock are recorded at the lower of cost, determined on the last-in, first-out method (LIFO), or market.

Mineral Exploration and Development Costs -- All costs related to the acquisition, exploration, and development of mineral deposits are capitalized until such time as (1) the Company commences commercial exploitation of the related mineral deposits at which time the costs will be amortized, (2) the related project is abandoned and the capitalized costs are charged to operations, or (3) when any or all deferred costs are permanently impaired. At December 31, 1997, none of the projects described in Notes 7 and 8 had reached the commercial exploitation stage. No indirect overhead or general and administrative costs have been allocated to any of the projects. In 1996 the Company adopted Statement of Financial Accounting Standards No. 121, "Accounting

for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed of" and has concluded that there is no impairment.

Refinery Plant, Pipeline and Equipment -- Refinery plant, pipeline, buildings and equipment are being depreciated using the straight-line method over useful lives of 3 to 15 years. Maintenance and repairs are charged to expense. Renewals and betterments are capitalized.

Other Assets -- Other assets include catalysts used in refinery operations, prepaid expenses, a note receivable and certain refinery assets which are being leased to a third party.

Environmental Liabilities -- Remediation costs are accrued based on estimates of known environmental remediation exposure. Such accruals are recorded even if uncertainties exist over the ultimate cost of the remediation. Ongoing environmental compliance costs, including maintenance and monitoring costs, are expensed as incurred.

Deferred Revenue -- Deferred revenue represents funds advanced by a supplier and customer for equipment purchases and is being amortized over a 15 year period.

Statements of Cash Flows -- On the statements of cash flows, cash includes cash held in the United States and Saudi Arabia. Significant noncash changes in financial position in 1997 include the issuance of 345,000 shares of common stock at \$1.00 per share for the conversion of \$345,000 of indebtedness (Note 9), as well as the issuance of stock and options for services, valued at a total of \$175,000, which is included in general and administrative expenses (Note 11). Transactions of this type in 1996 include a restructure of debt to include \$445,773 of accrued interest in the loan principal, as well as the issuance of stock and options for services, valued at a total of \$1,346,950, which is capitalized as a cost of the Al Masane Project (Note 7). Transactions of this type in 1995 include the write-off of a stockholder receivable to purchase 100,000 shares of common stock at \$1.00 per share and the issuance of 278,000 shares of common stock at \$1.00 per share for the cancellation of \$278,000 of indebtedness (Note 9).

Hedging Program -- In July 1994, South Hampton established a hedging program to help decrease the volatility of the price of fuel gas to the refinery. South Hampton purchased several commodity based derivative futures contracts during 1994. Gains and losses related to these contracts are recognized when the contracts expire. The natural gas market suffered severe price declines in the last few months of 1994 and into 1995, which resulted in net recognized losses of \$101,000 in 1995. These losses are included as a cost of refined product sales and processing in the consolidated statements of operations. Since the fuel prices decreased in 1995 and were expected to soften in the next year or two, the hedging program was discontinued in June 1995. In June 1997, the hedging program resumed and resulted in a net recognized gain of \$46,000 in 1997.

Net Income (Loss) Per Share -- In the fourth quarter of 1997, the Company adopted the provisions of Statement of Financial Accounting Standards No. 128, "Earnings per Share" (SFAS No. 128). In accordance with SFAS No. 128, the Company computes basic income per common share based on the weighted-average number of common shares outstanding. Diluted income per common share is computed based on the weighted-average number of common shares outstanding plus the number of additional common shares that would have been outstanding if dilutive potential common shares, consisting of stock options and shares issuable upon conversion of debt, had been issued (Note 15). Retroactive application, which is required by SFAS No. 128, did not result in restatement of 1995 or 1996 per share data.

Foreign Currency -- Assets and liabilities denominated in foreign currencies, principally Saudi Riyals, are translated at rates in effect at the time the transaction occurs. There has been no significant change in the exchange rate for Saudi Riyals to the United States dollar during the period covered by these financial statements. Due to the stability of the Saudi Riyal, the Company feels it has no material exposure to foreign currency risks and does not employ any practices to minimize any such risks. It is anticipated that its products in Saudi Arabia will be sold in US dollars.

Goodwill -- Goodwill acquired in connection with the acquisition of TOCCO in 1987 was fully amortized in 1997. The amount reflected in the balance sheet at December 31, 1996 is net of accumulated amortization of \$2,655,925.

Management Estimates -- The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that 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.

Stock-Based Compensation -- Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation" ("Statement No. 123") is effective for

years after 1995. Statement No. 123 establishes accounting and reporting standards for various stock-based compensation plans. Statement No. 123 encourages the adoption of a fair value based method of accounting for employee stock options, but permits continued application of the accounting method prescribed by Accounting Principles Board Opinion No. 25 ("Opinion 25"), "Accounting for Stock Issued to Employees." Entities that continue to apply the provisions of Opinion 25 are required to make pro forma disclosures of net income and earnings per share as if the fair value based method of accounting had been applied. Refer to Note 11.

NOTE 4 -- FAIR VALUE OF FINANCIAL INSTRUMENTS AND CONCENTRATION OF CREDIT RISK

At December 31, 1997, the Company's financial instruments included cash, cash equivalents, investments, accounts receivable, current obligations, and noncurrent liabilities. The fair values of these items approximate their carrying amounts at December 31, 1997. Accrued liabilities in Saudi Arabia consist primarily of accrued salary and benefits. Payment of these items is contingent on the Company's ability to obtain future financing. As such, a fair value cannot be reasonably estimated.

Financial instruments that are potentially subject to concentrations of credit risk consist of cash equivalents, short-term investments, and trade accounts receivable. The Company places its cash equivalents and short-term investments with high credit quality financial institutions.

South Hampton, the Company's only revenue producing asset, sells its products primarily to companies in the chemical and plastics industries. Downturns in these industries could negatively impact refinery operations in the future. South Hampton does not require collateral on its outstanding accounts

25

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

receivable balances. South Hampton's largest customer accounted for 10%, 17% and 25% of total sales in 1997, 1996 and 1995, respectively.

NOTE 5 -- CONTINGENCIES

The operations of the Company in Saudi Arabia have been, and may in the future be, affected from time to time in varying degree by political developments and laws and regulations, such as forced divestiture of assets; restrictions on production, imports and exports; price controls; tax increases and retroactive tax claims; expropriation of property, cancellation of contract rights and environmental regulations.

A major component of the Company's activities relates to the acquisition, exploration and development of mineral deposits. There can be no assurance that the Company will successfully develop any of the properties described in Notes 7 and 8, and, if developed, whether the mineral acquisition, exploration and development costs incurred will ultimately be recovered. The recovery of such costs is dependent upon a number of future events, some of which are beyond the control of the Company. The ability of the Company to develop any of these properties is dependent upon obtaining additional financing as may be required and, ultimately, its financial success depends on its ability to attain successful operations from one or more of its projects.

South Hampton, was a defendant in two lawsuits in two district courts in Jefferson County, Texas brought on July 21, 1993 and July 18, 1994 by two former employees of the Goodyear Tire & Rubber Company, seeking unspecified actual and punitive damages for certain alleged illness and diseases resulting from alleged exposure to certain chemicals during their employment with Goodyear. One of these lawsuits was settled in March 1997 and the other in January 1998. The cost to the Company was not significant. A new lawsuit by another former Goodyear employee was filed in a Jefferson County District Court on December 16, 1997 for unspecified actual and punitive damages for the same reasons as the other two. The outcome of this lawsuit is not expected to have a material effect on the Company's financial position, results of operations or liquidity.

South Hampton has been spending an increased amount of time and expense on environmental and regulatory functions and compliance. It is South Hampton's policy to accrue costs associated with regulatory compliance when those costs are reasonably determinable. In 1993, while remediating a small spill area, The Texas Natural Resources Conservation Commission ("TNRCC") requested that the refinery drill a well to check for groundwater contamination under the spill area. Based on the results, estimated costs of \$60,000 were accrued at December 31, 1996 to cover the recovery and remediation activity expected to take place in 1997. However, no action was taken other than further study, and another \$50,000 was accrued at December 31, 1997, for a total of \$110,000. This amount is considered adequate in that various alternative and less expensive means of recovery are being developed by the South Hampton. Approximately \$85,000 has been expended over a three year period to develop recovery alternatives. The consulting engineers expect approximately 10,000 barrels of recoverable material may be available to South Hampton for use in their refining process, but no reduction has been made in the accrual for estimated remediation costs due to the uncertainties relating to the recovery process.

In August 1997, the TNRC notified South Hampton that it had violated various rules and procedures and has proposed administrative penalties totaling \$709,408 and recommended that South Hampton undertake certain actions necessary to bring its operations at the refinery into compliance. The violations generally relate to various air and water quality issues. South Hampton intends to vigorously defend against this action on the basis that the allegations are in error or involve matters that are relatively minor in importance.

In addition to the various Environmental Protection Agency and TNRC air, water and solid waste regulations, South Hampton is also subject to the regulations of the U.S. Department of Transportation,

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

the Occupational, Health and Safety Administration and the Texas General Land Office, among others. In response to various regulations from these and other agencies, South Hampton has developed OPA-90 Emergency Response Plans for the pipeline and the refinery, and is in the process of voluntarily adopting the requirements of the OSHA Process Safety Management rules. Approximately \$37,000, \$35,000 and \$80,000 was spent in 1997, 1996 and 1995, respectively, on development of this OSHA program. The program is approximately 75% completed and is expected to be completed in 1998 at an additional cost of approximately \$37,000. Due to the uncertain timing and scope of the additional work, no accruals have been provided.

At December 31, 1997, the Company had not made all of the surface rental payments due to the government of Saudi Arabia under the terms of the Al Masane Project lease. The past due amount of these rent payments was approximately \$426,000 but, in February 1998, a payment in full of approximately \$469,000 was made. In addition, the Company has not complied with certain statutory reporting requirements in Saudi Arabia. Management of the Company believes that the lack of compliance with these requirements will not have any effect on the Company's planned operations in Saudi Arabia.

At December 31, 1997, South Hampton had a \$100,000 letter of credit in support of payment for purchases of natural gas used in the refinery from its main supplier.

NOTE 6 -- INVENTORIES

Inventories include the following:

<TABLE>
<CAPTION>

	DECEMBER 31,	
	1997	1996
<S>	<C>	<C>
Refinery feedstock.....	\$ 86,591	\$ --
Refined products.....	461,729	565,346
	-----	-----
Total inventories.....	\$548,320	\$565,346
	=====	=====

</TABLE>

At December 31, 1997, LIFO value approximated current cost. At December 31, 1996, current cost exceeded LIFO value by approximately \$163,000.

NOTE 7 -- MINERAL EXPLORATION AND DEVELOPMENT COSTS IN SAUDI ARABIA

In the accompanying consolidated financial statements, the deferred development costs have been presented based on the related projects' geographic location within Saudi Arabia. This includes the "Al Masane Project"(the "Project") and "Other Interests in Saudi Arabia" which primarily pertains to the costs of rentals, field offices and camps, core drilling and labor incurred at the Wadi Qatan and Jebel Harr properties.

The Company has held exploration licenses for the Wadi Qatan and Jebel Harr areas in Saudi Arabia. Although the licenses have expired, the Saudi Arabian government has verbally advised the Company that they will be extended as long as mineral exploration is being carried out on the areas which they cover. When financing for the Al Masane project is completed, the Company anticipates applying for an exploration license for an area of 2,800 square kilometers which will include the original Greater Al Masane area plus the Wadi Qatan and Jebel Harr areas. The Company has had positive results from its exploration work at these sites; however, it has directed limited amounts of time and resources to them in recent years while it negotiated with the Saudi government for the Al Masane lease. The Company does not intend to abandon these sites.

On April 26, 1993, the Council of Ministers passed a resolution granting the Company a mining lease for the Al Masane Project, and on May 22, 1993, a Royal Decree was issued by the King. The initial period of

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

the mining lease is 30 years, which can be renewed for another period or periods, not to exceed 20 years. The lease area is 44 square kilometers in size. The lease agreement stipulates that the Company is to pay the Saudi government a surface rental of approximately \$117,000 a year. The Company made the first year's payment in August 1993. As of December 31, 1997, the Company had not paid for rentals of approximately \$426,000 but, in February 1998, a payment in full of approximately \$469,000 was made. A loan from the Saudi Industrial Development Fund ("SIDF"), was applied for on September 30, 1995, and conditional approval was received in December 1997. The Company intends to form a Saudi limited liability company to be owned 50% by the Company and 50% by the Al Mashreq Company for Mining Investments (Al Mashreq), and transfer the mining lease to it, free and clear of any lien interest the Saudi government has. The lease agreement stipulates that, after two years of profitable mine operations, a Saudi public stock company will be formed to which the limited liability company will transfer its interest in the Al Masane Project. The limited liability company will own no less than 50% of the stock in the public stock company. The Petroleum and Mineral Organization ("PETROMIN"), a company wholly-owned by the Saudi government, has an option to acquire up to 25% of the stock and the remaining interests not owned by the Company and Al Mashreq or acquired by PETROMIN are to be put out for public subscription to Saudi citizens.

The Company has an \$11 million interest-free loan from the Saudi Arabian government, the proceeds of which were used to fund the Project. The loan was scheduled to be repaid in ten annual installments beginning in 1984. None of the scheduled payments have been made. Pursuant to Article 18 of the Mining Lease Agreement, the Company intends to repay the loan in accordance with a repayment schedule to be agreed upon with the Saudi Arabian government from its share of Project cash flows. While the mining lease was granted in 1993, a rescheduling of the loan payments has not yet been negotiated. All of the Company's "movable and immovable" assets in Saudi Arabia are pledged as collateral for the loan.

On May 20, 1996, the Company entered into a Financial and Legal Services and Advice Agreement with two Saudi Arabian advisors to provide the following services in connection with the Al Masane mining project: (1) the formation of a Saudi limited liability company with the necessary capital to purchase the Company's interest in the mining lease and to pay its share of the project costs, (2) to finalize the required procedures for the issuance of an industrial license, (3) to finalize the necessary procedures to obtain the loan from the SIDF, (4) to apply for and receive loans from commercial banks necessary to finance the project and (5) to apply and obtain approval for the transfer of the mining lease to the limited liability company. As consideration for their services, the Company agreed to pay the two advisors \$10,000 each for the issuance of the industrial license and to pay one of them \$10,000 upon approval of the loan by the SIDF. The Company also agreed to issue them up to 2,000,000 shares of the Company's common stock and to grant them options to purchase up to 2,300,000 shares of the Company's common stock. The Company was obligated to issue such shares and options in designated amounts upon completion of each of the foregoing services. The options would have a five-year term commencing on the date of formation of the Saudi limited liability company with an exercise price of \$1.00 per share. On December 3, 1996, the industrial license was issued to the Company and its Saudi Arabian advisors, and the Company has paid \$20,000 in cash and is obligated at December 31, 1997 for the issuance of 300,000 shares of common stock and stock options for 345,000 shares at \$1.00 per share. The Agreement was terminated in August 1997 and negotiations are being held to complete a new agreement.

Phase I of the work on the Project (sinking shaft, tunneling and drilling) was completed in April 1981. Since that time, there have been a series of project feasibility studies in 1982, 1984, 1989, 1992, and 1994, conducted by Watts, Griffis and McQuat Limited, consulting geologist, indicating the commercial viability of the Project. The 1994 report, and an update prepared in 1996, estimates proven and probable reserves of copper, zinc, silver and gold of 7.2 million tonnes in the Project with the potential to increase

28

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

these reserves with further exploration. The report projects production of the proven and probable reserves over a ten-year period. A cash flow projection was made based on the assumption that 50% of the financing of the project will come from loans from the Saudi Industrial Development Fund, 25% from bank loans, and 25% from equity financing of the new Saudi limited liability company. Revenues were estimated utilizing projected mineral prices from a third party pricing expert. The report projected positive net cash flows to the Company of \$47.5 million over the life of the Project. According to the provisions of Article 46 of the Saudi Mining Code, no taxes will be payable to the Saudi government during the first stage of operations on a mining lease, which is the period of five years starting from the earlier of (a) the date of the first sale of products or (b) the beginning of the fourth year since the issue of the lease.

Deferred development costs of the Al Masane Project at December 31, 1997, 1996 and 1995, and the changes in these amounts for each of the three years then ended are detailed below:

<TABLE>
<CAPTION>

	BALANCE AT DECEMBER 31, 1997	ACTIVITY FOR 1997	BALANCE AT DECEMBER 31, 1996	ACTIVITY FOR 1996	BALANCE AT DECEMBER 31, 1995	ACTIVITY FOR 1995
<S>	<C>	<C>	<C>	<C>	<C>	<C>
Property and equipment:						
Mining equipment.....	\$ 2,160,206		\$ 2,160,206		\$ 2,160,206	
Construction costs.....	3,140,493		3,140,493		3,140,493	
Total.....	5,300,699		5,300,699		5,300,699	
Other costs:						
Labor, consulting services and project administration costs....	19,145,296	\$562,523	18,582,773	\$1,942,586	16,640,187	\$616,912
Materials and maintenance.....	6,168,661	737	6,167,924	914	6,167,010	5,326
Feasibility study.....	2,907,771	76,329	2,831,442	41,455	2,789,987	163,513
Total.....	28,221,728	639,589	27,582,139	1,984,955	25,597,184	785,751
	\$33,522,427	\$639,589	\$32,882,838	\$1,984,955	\$30,897,883	\$785,751

</TABLE>

The deferred development costs of the "Other Interests in Saudi Arabia", in the total amount of approximately \$2.4 million, consist of approximately \$1.5 million associated with the Greater Al Masane area and the balance of approximately \$900,000 is associated primarily with the Wadi Qatan and Jebel Harr areas. In the event an exploration license for these areas is not granted, the entire amount of deferred development costs relating thereto would be written off.

NOTE 8 -- MINERAL PROPERTIES IN THE UNITED STATES

The Company has voting rights of approximately 52% and directly owns approximately 44% of the outstanding common stock of Pioche. During 1988, 634,223 shares of Pioche stock were deemed acquired through in-substance foreclosure on a \$114,537 note due from the issuer's estate. The original date of the note was May 31, 1985, and the note was due on May 31, 1995; however, management of the Company extended the due date to December 31, 1998 to allow the estate the opportunity to pay off the note. Until the note is paid, the Company has the voting rights to these shares. At this time, it is not possible to determine whether the issuer's estate will be able to repay the note when due. If the note is not repaid, the Company could take ownership of the shares. At December 31, 1996, the Company determined the loan was not likely to be repaid, and has consolidated the accounts of Pioche in the accompanying financial statements for 1997 and 1996. Previously, the investment in Pioche was accounted for on the equity method. The consolidation of Pioche increased total assets at December 31, 1996 by approximately \$1,200,000 and had no effect on the net loss reported for 1996.

29

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

The principal assets of Pioche are an undivided interest in 48 patented and 81 unpatented mining claims and a 300 ton-per-day mill located on the aforementioned properties in the Pioche Mining District in southeastern Nevada. Due to the lack of capital, the properties held by Pioche have not been commercially operated for approximately 35 years. During 1994, Pioche attempted to drill a core hole on this property. The core hole was intended to go down to 1,500 feet but encountered formation problems at 700 feet and further drilling had to be abandoned. A new site will be selected and management expects a second core hole to be drilled when financing becomes available. In late 1996, Pioche was extended a proposal from a prominent mining company for the lease of its mining claims and on October 1997, an "Exploration Agreement and Option to Purchase" was entered into. The agreement provides for annual payments to Pioche of \$50,000 for seven years until, or unless, an option is exercised to purchase an 85% interest in the mining claims for \$3,000,000. The mining company will pay all annual taxes and claim rentals and has agreed to expend at least \$50,000 in exploration work each year and to drill at least one hole during the first year. The agreement can be terminated upon 60 days written notice from the mining company.

The Company has an option to buy 720,000 shares (approximately 10% of the outstanding shares) of Pioche common stock at \$0.20 per share. The option expires on June 1, 2002.

On June 30, 1997, Pioche entered into an option agreement to lease the mill for one year, or as long thereafter as there are operations within the mill and /or active milling of ore. The lease provides for lease payments of \$1.00 per short ton of ore milled with a maximum daily payment of \$300 and a minimum daily payment of \$100.

NOTE 9 -- NOTES PAYABLE, LONG-TERM DEBT AND LONG-TERM OBLIGATIONS

Notes payable, long-term debt and long-term obligations at December 31 are summarized as follows:

<TABLE>
<CAPTION>

	1997	1996
	-----	-----
<S>	<C>	<C>
Notes payable:		
Secured note to Saudi Arabian government. See (B).....	\$11,000,000	\$11,000,000
Unsecured note to a Saudi investor. See (D).....	13,280	13,280
Unsecured note to a Saudi investor. See (E).....	350,000	350,000
Other.....	12,500	12,500
	-----	-----
Total.....	\$11,375,780	\$11,375,780
	=====	=====
Long-term debt:		
Revolving bank note. See (A).....	\$ 1,590,000	\$ 1,890,000
Unsecured note to a Saudi company. See (C).....	1,945,773	1,945,773
Unsecured notes to foreign investors. See (F).....	498,000	598,000
Bank note. See (G).....	--	103,068
	-----	-----
Total.....	4,033,773	4,536,841
Less current portion.....	(598,000)	(992,729)
	-----	-----
Total.....	\$ 3,435,773	\$ 3,544,112
	=====	=====
Long-term obligations:		
Noninterest-bearing note to a supplier and customer for capital improvements. See (H).....	\$ 24,000	\$ 128,683
Deferred compensation contracts. See (I).....	35,120	57,230
	-----	-----
Total.....	59,120	185,913
Less current portion.....	(37,915)	(150,904)
	-----	-----
Total.....	\$ 21,205	\$ 35,009
	=====	=====

</TABLE>

(A) In 1990, South Hampton and a bank entered into an Amended and Restated Credit Agreement ("the Agreement"). Funding under the Agreement was provided in two facilities: Facility A in the principal amount of \$4,400,000, funded in a lump-sum, and Facility B in the principal amount of up to \$1,500,000, to be used by South Hampton for working capital purposes and support of feedstock purchases. Facility B was fully drawn down in the form of letters of credit. In 1992, the bank drew on the letters of credit provided by a related party of the Company (see (C) below.)

On October 15, 1996, South Hampton and the bank agreed to amend and restate the Agreement (the "Restated Agreement"). South Hampton executed a new Promissory Note in the original principal amount of \$1,965,000 having a December 31, 1998 maturity date (extended in March 1998 to December 31, 1999) and bearing interest at the rate of one percent above the prime lending rate in effect at the bank's New York office payable monthly in arrears on the last day of each month. Advances under the Restated Agreement are not to exceed the lesser of \$1,965,000 or the borrowing base, which is calculated as the cash collateral account and eligible receivables and inventory. Minimum principal payments of \$75,000 are to be made, payable by the last day of each quarter commencing December 31, 1996. As in the previous Agreement, South Hampton has agreed to collect all receivables through a cash collateral account at a local bank. Various restrictions have been placed on how funds may be spent by South Hampton and periodic reports must be provided to the bank. Under certain guidelines, the Restated Agreement permits certain cash distributions to Saudi Fal Co., Ltd. ("Saudi Fal"), TOCCO, the Refining Company, and the Company. The note is collateralized by all of the assets of TOCCO and its subsidiaries and a pledge of TOCCO common stock owned by the Refining Company. The Restated Agreement contains certain financial covenants, including a minimum current ratio and fixed charges coverage ratio.

(B) The Company has an interest-free loan of \$11,000,000 from the Saudi Arabia Ministry of Finance and National Economy, the proceeds of which were used to finance the development phase of the Al Masane Project. The loan was repayable in ten equal annual installments of \$1,100,000, with the initial installment payable on December 31, 1984. None of the ten scheduled payments have been made. Pursuant to the mining lease agreement covering the Al Masane Project, the Company intends to repay the loan in accordance with a repayment schedule to be agreed upon with the Saudi Arabian government from its share of Project cash flow. An agreement has not yet

been reached regarding either the rescheduling or source of these payments. The loan is collateralized by all of the Company's "movable and immovable" assets in Saudi Arabia.

- (C) In 1990, Saudi Fal, a Saudi company owned by a shareholder of the Company, agreed to issue a guarantee of \$1,500,000 securing a letter of credit facility to enable South Hampton to buy feedstock. In return for the guarantee, Saudi Fal was given an option to purchase all of the outstanding stock of TOCCO. The option was not exercised and has expired. On March 31, 1992, the \$1,500,000 guarantee was not renewed by Saudi Fal. As a result, the bank drew on the letter of credit provided by Saudi Fal for its guarantee and applied the \$1,500,000 to reduce the principal amount of the bank note. The note is now owed by South Hampton to Saudi Fal. On October 15, 1996, South Hampton and Saudi Fal agreed to restructure the loan terms, whereby the accrued interest to date of \$445,773 was added to principal, the interest rate was set at prime plus 1%, and the maturity date was changed to December 31, 1998. In March 1998, the maturity date was extended to December 31, 1999. This new note has a second lien position behind the bank's position as discussed in (A) above and is convertible into 1,945,773 shares of common stock.
- (D) Represents a noninterest-bearing demand loan payable.
- (E) Represents an unsecured, noninterest-bearing advance made in 1984 to the Al Masane Project.

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

- (F) Represents loans payable to a stockholder of the Company for \$445,000, and the Company's president for \$53,000. \$200,000 is due in 1999, with interest payable at the LIBOR rate plus 2% at maturity. The remaining amounts are due on demand, with interest payable at the LIBOR rate plus 2%. Each loan provides for an option to convert the loan amount to shares of the Company's common stock at \$1.00 per share anytime within five years from the date of the loan. In December 1997, a relative of the Company's president and stockholder who had loaned \$300,000 to the Company in 1995, exercised the option and converted his loan amount, plus accrued interest of \$45,000, into common stock.
- (G) This note payable was collateralized by land, an office building, and all equipment and furniture and fixtures of TOCCO. As described in Note 10, the building collateralized by this note had been leased to a third party and, in June 1997, was sold and part of the proceeds was used by TOCCO to pay off this note.
- (H) Balance represents amount due under a note payable to an unrelated refining company that provided loans to South Hampton to fund certain refining processes. Repayment was to be made when certain feed rate criteria and number of days of operations had been reached. As of December 31, 1997, these criteria had been met and the loan is being repaid.
- (I) In connection with the acquisition of TOCCO, deferred compensation contracts between TOCCO and a certain former employee and one current employee were restructured, reducing the gross payments due under the original contracts. Default on payments due under the restructured agreements would invalidate the negotiated settlement amounts resulting in TOCCO being liable for the amounts due under the original contracts. TOCCO has complied with the terms of these contracts through 1997. However, if TOCCO were to default on these contracts, it would be liable for an additional amount of \$440,130. The recorded liability at December 31, 1997 and 1996 has been determined utilizing a discount rate of 8.0%.

Scheduled maturities of long-term debt and long-term obligations, which exclude current notes payable balances aggregating \$11,375,780, are as follows:

<TABLE>
<CAPTION>

<S>		<C>
1998.....		\$ 635,915
1999.....		3,456,978

Total.....		\$4,092,893
		=====

</TABLE>

Interest of \$305,007, \$186,190 and \$244,828 was paid in 1997, 1996 and 1995, respectively.

NOTE 10 -- COMMITMENTS

South Hampton leases vehicles and equipment for use in operations for approximately \$29,000 per month from a related party on a month to month basis. South Hampton incurred costs related to this agreement of approximately \$349,000, \$349,000 and \$316,000 in 1997, 1996 and 1995, respectively.

The Company incurred total rental expenses for office space and certain vehicles and equipment of approximately \$361,000, \$361,000 and \$302,000 in 1997, 1996 and 1995, respectively.

In February 1993, TOCCO entered into an agreement to lease to a third party a building with a net book value at December 31, 1996 of \$310,926 which TOCCO did not use in its operations. The lease was recorded as an operating lease and the building was included in Other Assets. As described in Note 9, the leased building was pledged as collateral for a note payable. In June 1997, the building was sold for approximately \$695,000. The sale resulted in a 10 year note receivable for \$610,000 bearing interest at 9%. The note is pledged to a bank. Miscellaneous income includes approximately \$25,000, \$102,000, and \$102,000 in 1997, 1996 and 1995, respectively of rental income pursuant to this lease. The gain on sale of approximately \$387,000 has been deferred, and is being recognized on the installment method as payments are received on the note. The note is included in Other Assets, net of the deferred gain.

32

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

A provision of the purchase agreement related to the acquisition of TOCCO by the Refining Company requires TOCCO to reserve up to 10% of its common stock to be available for sale to the employees of TOCCO on such terms and conditions and at such times as determined by TOCCO.

South Hampton has guaranteed a note for \$160,000 for a limited partnership in which South Hampton has a 19% interest.

NOTE 11 -- COMMON STOCK AND STOCK OPTIONS

At December 31, 1997, Saudi Arabian investors owned approximately 64% of the Company's outstanding common stock.

Common Stock -- The proceeds from common stock sales are used to finance mineral exploration and development activities in Saudi Arabia and general and administrative expenses in the United States. Agreements relating to certain stock sold to investors provide that shares may not be traded in United States markets unless registered under the United States Securities Act of 1933 or unless they are sold pursuant to an available exemption from registration.

Notes receivable from stockholders for the purchase of common stock of \$126,000 at December 31, 1997 and 1996 represents a note from a director and officer which matures on December 31, 1998. Notes receivable from stockholders are classified as a reduction of stockholders' equity.

Stock Options -- Under the terms of the Company's Employee Stock Option Plan (the "Employee Plan"), incentive options are granted at the market price of the stock on the date of grant and non-incentive options are granted at a price not less than 85% of the market price of the stock on the date of grant. The Employee Plan was adopted on May 16, 1983 for a term of ten years. At the Company's annual stockholders meeting on December 29, 1992, the stockholders approved an extension of the term of the Employee Plan for another ten years to May 16, 2003 and also approved an increase in the number of shares reserved for issuance thereunder from 250,000 to 500,000. On November 5, 1997, the Employee Plan was registered with the Securities and Exchange Commission.

To enhance the Company's ability to obtain and retain qualified directors, it instituted the 1987 Non-Employee Director Stock Option Plan (the "Non-Employee Director Plan") which provides for each non-employee director to receive an option for 10,000 shares of common stock upon election to the board of directors with the exercise price equal to the fair market value of the stock at the date of grant. The number of shares reserved for issuance under this plan is 100,000. The Non-Employee Director Plan was instituted in 1987 for a duration of ten years and in 1997 it expired. A new plan may be instituted at a later date.

Under the above plans, 325,000 shares were reserved for grant at December 31, 1997. The options for the Employee Plan vest at such times and in such amounts as is determined by the Compensation Committee of the Board of Directors at the date of grant. The options for the Non-Employee Director Plan vest in cumulative annual installments of 20% beginning one year from the date of grant. The options for both plans are exercisable for a period of ten years.

In 1995, the Company wrote off a receivable from a company controlled by a director of the Company in the amount of \$100,000 resulting from the exercise of stock options.

In 1995, three foreign investors and the president of the Company loaned the Company \$668,000 and \$53,000, respectively (See Note 9). The agreements provide that the lender would have the option, at anytime within five years from the date of the loan, to convert the debt plus accrued interest into restricted shares of the Company's common stock at \$1.00 per share. In September 1995, one of the investors exercised his option and converted \$123,000 of his loan to 123,000 shares of common stock outstanding.

33

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

In October 1995, the Board of Directors approved an option for the president of the Company to exchange \$400,000 of his unpaid salary for restricted shares of the Company's common stock at \$1.00 per share. The options do not expire and they were exercisable immediately upon grant.

On May 20, 1996, the Company entered into a Financial and Legal Services and Advice Agreement with two Saudi Arabian advisors who assisted the Company with the Al Masane Project (See Note 7). The Agreement was terminated by the Company in August 1997. The Agreement provided for consideration to the advisors of up to 2,000,000 shares of the Company's common stock and options to purchase up to 2,300,000 shares of common stock at \$1.00 per share. The options were to be granted in designated amounts upon the completion of various obligations by the advisors. The options were immediately exercisable upon grant and would have a five year term beginning on the date of the formation of the Saudi limited liability company. At December 31, 1996, 300,000 shares of common stock, valued at \$550,000, and options to purchase 345,000 restricted shares, valued at \$796,950, had been earned under the Agreement.

For stock options granted to employees and directors at an exercise price below market price on the date of grant, the Company records an expense equal to the difference between the exercise price and the market prices on the date of grant. An expense is also recorded for the difference between sales price and market price for stock sold to employees and directors, not pursuant to options, at below market prices.

For the options to purchase 668,000 shares of stock granted to investors during 1995, the Company recognized an expense of \$76,500, which is included in general and administrative expense in the Company's results of operations for the year ended December 31, 1995. For the options to purchase 400,000 shares of stock granted to the Company's president in 1995, the Company recorded compensation expense in the amount of \$74,900, which is included in general and administrative expense in the Company's results of operations for the year ended December 31, 1995.

During 1997, the Company granted options to purchase 100,000 shares of stock and issued 50,000 shares of stock for services to two directors of the Company. The Company recorded compensation expense in the amount of \$175,000, which is included in general administrative expense in the Company's results of operations for the year ended December 31, 1997. The Company has adopted only the disclosure provisions of Statement No. 123, as discussed in Note 3. Therefore, compensation expense for stock options granted to employees is measured as the excess, if any, of the quoted market price of the Company's stock at the date of grant over the amount an employee must pay to acquire the stock. If the Company recognized compensation expense based upon the fair value at the grant date for options granted to employees in 1997 and 1995 (none were granted in 1996), the Company's 1997, 1996 and 1995 net income (loss) and income (loss) per share would be the pro forma amounts indicated as follows:

<TABLE>
<CAPTION>

	1997	1996	1995
	-----	-----	-----
<S>	<C>	<C>	<C>
Net income (loss)			
As reported.....	\$818,364	\$(390,896)	\$(369,232)
Pro forma.....	\$635,714	\$(390,896)	\$(726,332)
Income (loss) per common share -- basic and diluted			
As reported.....	\$.04	\$ (.02)	\$ (.02)
Pro forma.....	\$.03	\$ (.02)	\$ (.04)

</TABLE>

The fair value of these options was estimated at the date of grant using the Black-Scholes option pricing model with the following weighted-average assumptions: expected volatility of 85 percent; risk-free interest rate of 6 percent; no dividend yield; and expected lives of three to 10 years.

The pro forma amounts presented are not representative of the amounts that will be disclosed in the future because they do not take into effect pro forma expenses related to grants before 1995.

Additional information with respect to all options outstanding at December 31, 1997, and changes for the three years then ended was as follows:

<TABLE>
<CAPTION>

	1995

SHARES	WEIGHTED AVERAGE EXERCISE PRICE
-----	-----

<S>	<C>	<C>
Outstanding at beginning of year.....	215,000	\$1.83
Granted.....	1,121,000	1.00
Exercised.....	(123,000)	1.00
	-----	-----
Outstanding at end of year.....	1,213,000	\$1.15
	=====	=====
Options exercisable at December 31, 1995.....	1,163,500	\$1.12
	=====	=====

</TABLE>

<TABLE>
<CAPTION>

	1996	
	SHARES	WEIGHTED AVERAGE EXERCISE PRICE
<S>	<C>	<C>
Outstanding at beginning of year.....	1,213,000	\$1.15
Granted.....	345,000	1.00
	-----	-----
Outstanding at end of year.....	1,558,000	\$1.11
	=====	=====
Options exercisable at December 31, 1996.....	1,550,000	\$1.10
	=====	=====

</TABLE>

Weighted average fair value per share of options granted in 1996 was \$2.31.

<TABLE>
<CAPTION>

	1997	
	SHARES	WEIGHTED AVERAGE EXERCISE PRICE
<S>	<C>	<C>
Outstanding at beginning of year.....	1,558,000	\$1.11
Granted.....	110,000	1.14
Forfeited.....	(10,000)	3.50
Exercised.....	(10,000)	1.38
	-----	-----
Outstanding at end of year.....	1,648,000	\$1.10
	=====	=====
Options exercisable at December 31, 1997.....	1,639,000	\$1.09
	=====	=====

</TABLE>

Weighted average fair value per share of options granted in 1997 was \$1.77.

Information about stock options outstanding at December 31, 1997 is summarized as follows:

<TABLE>
<CAPTION>

	OPTIONS OUTSTANDING		
	NUMBER OUTSTANDING	WEIGHTED AVERAGE REMAINING CONTRACTUAL LIFE	WEIGHTED AVERAGE EXERCISE PRICE
<S>	<C>	<C>	<C>
\$0 to 1.....	1,443,000	7.1 years	\$1.00
\$1 to 2.....	165,000	7.3 years	1.55
\$2 to \$3.75.....	40,000	5.7 years	2.85
	-----	-----	-----
	1,648,000		\$1.10
	=====		=====

</TABLE>

<TABLE>
<CAPTION>

	OPTIONS EXERCISABLE	
	NUMBER EXERCISABLE	WEIGHTED AVERAGE EXERCISE PRICE
<S>	<C>	<C>
\$0 to 1.....	1,443,000	\$1.00
\$1 to 2.....	165,000	1.55
\$2 to \$3.75.....	31,000	2.84
	-----	-----

1,639,000 \$1.09
 ===== =====

</TABLE>

NOTE 12 -- INCOME TAXES

The income (loss) before income taxes was \$818,364, (\$390,896) and (\$369,232) for the years ended December 31, 1997, 1996 and 1995, respectively.

Income tax expense (benefit) for the years ended December 31, 1997, 1996 and 1995 differs from the amount computed by applying the applicable U.S. corporate income tax rate of 34% to net income (loss) before income taxes. The reasons for this difference are as follows:

<TABLE>
 <CAPTION>

	1997	1996	1995
	-----	-----	-----
<S>	<C>	<C>	<C>
Income taxes at U.S. statutory rate.....	\$ 278,244	\$(132,905)	\$(125,539)
Goodwill amortization.....	39,252	94,228	95,303
Net operating losses carried forward (utilized).....	(326,839)	37,924	25,731
Other items.....	9,343	753	4,505
	-----	-----	-----
Total tax expense.....	\$ --	\$ --	\$ --
	=====	=====	=====

</TABLE>

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities for 1997, 1996 and 1995 were as follows:

<TABLE>
 <CAPTION>

	DECEMBER 31,		
	-----	-----	-----
	1997	1996	1995
	-----	-----	-----
<S>	<C>	<C>	<C>
Deferred tax liabilities:			
Refinery plant, pipeline and equipment.....	\$ (323,513)	\$ (287,845)	\$ (368,385)
Deferred tax assets:			
Accounts receivable.....	45,967	57,284	49,544
Mineral interests.....	196,446	196,446	196,446
Accrued liabilities.....	49,341	32,300	--
Net operating loss carryforwards (NOLs).....	10,943,970	11,333,611	11,274,638
Tax credit carryforwards.....	147,501	221,322	651,504
	-----	-----	-----
Gross deferred tax assets.....	11,383,225	11,840,963	12,172,132
Valuation allowance.....	(11,059,712)	(11,553,118)	(11,803,747)
	-----	-----	-----
Net deferred tax assets.....	323,513	287,845	368,385
	-----	-----	-----
Net deferred taxes.....	\$ --	\$ --	\$ --
	=====	=====	=====

</TABLE>

During 1995, the Company's gross deferred tax asset increased by \$2,003,157 to \$12,172,132 at December 31, 1995. The primary reason for this increase in the gross deferred tax asset is due to a restatement of NOLs from prior years. There was no change in judgment about the Company's ability to realize its net deferred tax asset; therefore, the valuation allowance was increased by a corresponding amount. If certain substantial changes in the Company's ownership should occur, there would be an annual limitation on the amount of tax carryforwards which could be utilized.

At December 31, 1997, the Company had approximately \$32,300,000 of net operating loss carryforwards and approximately \$148,000 of general business credit carryforwards. These carryforwards expire during the years 1998 through 2011. In addition, the Company has minimum tax credit carryforwards of approximately \$49,000 that may be carried over indefinitely. Approximately \$1,700,000 of the net operating loss carryforwards and \$13,000 of the general business credit carryforwards are limited to the net income of TOCCO. Approximately \$5,900,000 of the net operating loss carryforwards are limited to the net income of the Coal Company.

The Company has no Saudi Arabian tax liability.

NOTE 13 -- SEGMENT INFORMATION

The Company has operations in two industry segments and geographic regions. Its refinery operations represent the significant portion of its current operating results and are exclusively in the United States, whereas its mining operations, conducted mainly in Saudi Arabia, mostly relate to costs which have been deferred during the development phase of these operations. The only mining operations conducted in the United States relate to the Company's subsidiary, Pioche. The Company has no significant corporate activities.

Since a substantial portion of the Company's mineral properties and interests are located outside of the United States, its business and properties are subject to foreign laws and foreign conditions, with the attendant varying risks and advantages. Foreign exchange controls, foreign legal and political concepts, foreign government instability, international economics and other factors create risks not necessarily comparable with those involved in doing business in the United States.

For 1997, 1996 and 1995, essentially all activity on the Company's consolidated statement of operations relates to the refinery. The 1997, 1996 and 1995 results include \$39,475, \$33,944 and \$54,063, respectively, of unallocated costs recorded in general and administrative expenses related to the Saudi Arabian operations. The 1997, 1996 and 1995 results include immaterial amounts of interest expense related to notes payable that relate to the Saudi Arabian mining operations. All items included in the Company's consolidated balance sheet related to the Saudi Arabian operations are specifically identified on the face of the consolidated balance sheet with the exception of notes payable which have been identified in Note 9.

NOTE 14 -- RELATED PARTY TRANSACTIONS

The Company shares office facilities and certain expenses with companies owned by the chairman of the Company. At December 31, 1997 and 1996, these companies did not owe any amounts to the Company.

Noncurrent Accrued Liabilities in Saudi Arabia in the consolidated balance sheet represent amounts payable to the Company's president.

Other significant related party transactions have been addressed in the related notes to the consolidated financial statements. In particular, see Notes 9 and 11 for additional information.

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

NOTE 15 -- NET INCOME (LOSS) PER COMMON SHARE

Net income per share for 1997 has been calculated as follows:

<TABLE>
<CAPTION>

	NET INCOME	WEIGHTED AVERAGE SHARES OUTSTANDING	PER SHARE
	-----	-----	-----
<S>	<C>	<C>	<C>
Basic income per share.....	\$818,364	21,306,040	\$.04
Dilutive effect of stock options.....	--	711,612	--
	-----	-----	-----
Diluted income per share.....	\$818,364	22,017,652	\$.04
	=====	=====	=====

</TABLE>

In 1996 and 1995, the effect of stock options and convertible debt was anti-dilutive. Accordingly, loss per share is calculated by dividing the net loss by the weighted average shares outstanding. In 1997, the effect of assumed debt conversions is anti-dilutive.

REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS ON SCHEDULES

Board of Directors and Stockholders
Arabian Shield Development Company

In connection with our audit of the consolidated financial statements of Arabian Shield Development Company and Subsidiaries referred to in our report dated March 13, 1998, which is included in the annual report to stockholders in Part II of this Form 10-K, we have also audited Schedule II at December 31, 1997 and 1996 and for the years then ended. In our opinion, this schedule presents fairly, in all material respects, the information required to be set forth therein. Our report on the financial statements referred to above includes an explanatory paragraph which discusses that there is substantial doubt about the Company's ability to continue as a going concern.

SCHEDULE II
ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

VALUATION AND QUALIFYING ACCOUNTS
THREE YEARS ENDED DECEMBER 31, 1997

<TABLE>
<CAPTION>

DESCRIPTION	BEGINNING BALANCE	CHARGED (CREDITED) TO EARNINGS	DEDUCTIONS	ENDING BALANCE
Allowance for Deferred Tax Asset				
December 31, 1995.....	\$ 9,789,307	\$2,014,440	\$ --	\$11,803,747
December 31, 1996.....	11,803,747	179,553 (a)	(430,182)	11,553,118
December 31, 1997.....	11,553,118	-- (b)	(326,839)	11,059,712
		(a)	(166,567)	

</TABLE>

(a) Expiration of carryforwards

(b) Credit to earnings

DIRECTORS

John A. Crichton
Chairman of the Board
Arabian Shield Development Company
Dallas, Texas

Hatem El-Khalidi
President and Chief Executive Officer
Arabian Shield Development Company
Jeddah, Saudi Arabia

Mohammed O. Al-Omair
Executive Vice President
Saudi Fal Group of Companies
Riyadh, Saudi Arabia
(Investments)

Ghazi Sultan
Chairman
Sultan Group of Companies
Jeddah, Saudi Arabia
(Investments and marble mining)

EXECUTIVE OFFICERS

John A. Crichton
Chairman of the Board

Hatem El-Khalidi
President and Chief Executive Officer

Jonathan Cocks
Vice President

Drew Wilson, Jr.
Secretary/Treasurer

Nicholas N. Carter
President of Texas Oil and Chemical Co. II, Inc.

TRANSFER AGENT AND REGISTRAR

Harris Trust

STOCK LISTING

NASDAQ National Market System
Symbol ARSD

FORM 10-K

Single copies of the Annual Report on Form 10-K which the Company has filed with the Securities and Exchange Commission can be obtained by stockholders without charge by writing to Arabian Shield Development

Company, Suite 175, 10830 North Central Expressway, Dallas, Texas
75231, Attention: Secretary.

[ARABIAN SHIELD LOGO]

<TABLE>

<S>

General Office:

Field Office:

Transfer Agent:

</TABLE>

<C>

10830 North Central Expressway, Suite 175, Dallas, Texas
75231

P.O. Box 1516, Jeddah, Saudi Arabia

Harris Trust

<TABLE> <S> <C>

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<RESTATED>

<MULTIPLIER> 1,000

<S>

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<PERIOD-END>

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