

SECURITIES AND EXCHANGE COMMISSION

Washington, D. C. 20549

(Mark One)

[X] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 [FEE REQUIRED]

For the fiscal year ended December 31, 1994

or

[] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 [NO FEE REQUIRED]

For the transition period from _____ to _____
Commission file number 0-6247

ARABIAN SHIELD DEVELOPMENT COMPANY
(Exact name of registrant as specified in its charter)

DELAWARE 75-1256622
(State or other jurisdiction of (I.R.S. Employer
incorporation or organization) Identification No.)

10830 North Central Expressway
Suite 175 75231
Dallas, Texas (Zip Code)
(Address of principal executive offices)

Registrant's telephone number, including area code: (214) 692-7872

Securities registered pursuant to Section 12(b) of the Act:

None

Securities registered pursuant to Section 12(g) of the Act:

Common Stock, par value \$0.10 per share
(Title of Class)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes X No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. []

Number of shares of registrant's Common Stock, par value \$0.10 per share, outstanding as of March 20, 1995: 19,878,494.

The aggregate market value on March 20, 1995 of the registrant's voting securities held by non-affiliates was \$23,107,208.

DOCUMENTS INCORPORATED BY REFERENCE

- (a) Selected portions of the registrant's Annual Report to Stockholders for the year ended December 31, 1994. - Parts II and IV
- (b) Selected portions of the registrant's definitive Proxy

PART I

Item 1. Business.

General

Arabian Shield Development Company (the "Company") was organized as a Delaware corporation in 1967 and is principally engaged in the business of developing its undeveloped mineral properties. None of the undeveloped mineral properties are currently producing and significant capital expenditures will be necessary before any commercial operations are commenced. In an updated full bank feasibility study of the Al Masane lease area, which is under a 30-year mining lease to the Company, conducted in 1994 by an independent mining consulting firm, the consultants estimate the total capital costs of the Al Masane project to be \$81.3 million. The Company will diligently pursue the financing of the project so that commercial production can begin in the fourth quarter of 1996, 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.

The Company, through its indirect wholly-owned subsidiary, South Hampton Refining Company ("South Hampton"), owns and operates a petroleum refinery which is the Company's only significant revenue producing asset. South Hampton has scheduled short-term and current portions of long-term debt obligations which exceed its ability to repay from cash on hand and internally generated funds. To satisfy its current debt obligations in an orderly manner, South Hampton will need to renew certain debt obligations, achieve an increase in cash flow from the refinery and/or receive funds from the Company from future sales of the Company's Common Stock. See Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations for further discussion of these matters.

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 jointly holds with National Mining Company, a private Saudi company ("National Mining"), exploration licenses for the Wadi Qatan and Jebel Harr areas in Saudi Arabia. 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 is planning to apply for formal extensions of these licenses in 1995. Although the exploration licenses were awarded

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jointly to the Company and National Mining, the exploration work on the license areas has been carried on exclusively by the Company.

The Company has had discussions with Chevron Chemical Company regarding the Company's proposal to purchase 5,000 barrels per day of mixed pentanes from an Aromax petrochemical project to be built in Jubail, Saudi Arabia by Chevron Chemical in joint venture with Saudi Venture Capital Group (SVCS). The Company and some Saudi joint venture partners, all of whom are directors and/or stockholders of the Company, contemplate building a processing plant located next to the Aromax plant in Saudi Arabia. As proposed, the Company would have a 25% interest in the joint venture. Chevron Chemical advised the Company by letter that Chevron Chemical and SVCS have jointly agreed to commit to supply the joint venture's proposed pentane project with up to 5,000 barrels per day of mixed pentane feedstock. Engineering and marketing studies of the project have been made by outside consultants which reflect positive results. Planning has begun toward the construction and operation of the Aromax plant and the joint venture's processing plant. Construction is estimated to be completed in late 1996. The Company will begin applying to the Saudi government for a license for the project when the Aromax project receives final approval from the Saudi government.

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 designs for a state of the art zinc refinery. Sherritt's zinc pressure leach technology provides significant advantages over the other existing zinc production processes, including having the reputation as the most favored technology for environmental considerations. In the study Sherritt concludes, after considering all of the presently, identifiable elements, that these elements offer a strong potential for the project and enhance the concept. Sherritt encourages the Company to carry out further studies toward the implementation of the project.

United States Activities. American Shield Refining Company, a wholly owned subsidiary of the 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, indirectly through South Hampton, owns all of the capital stock of Gulf States Pipeline Company, Inc. ("Gulf States"). South Hampton owns and operates a petroleum refinery

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near Silsbee, Texas. Gulf States 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 owns all of the capital stock of American Shield Coal Company (the "Coal Company") and beneficially owns approximately 55%, and directly owns approximately 46%, of the capital stock of an inactive Nevada mining company, Pioche-Ely Valley Mines, Inc. ("Pioche-Ely Valley").

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 pre-feasibility mining study was conducted at Al Masane by the mining consulting firm of Watts, Griffis and McOuat 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

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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:

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<TABLE>
<CAPTION>

| Zone | Reserve (Tonnes) | Copper (%) | Zinc (%) | Gold (g/t) | Silver (g/t) |
|-------------------|---------------------|---------------|-------------|---------------|-----------------|
| <S> <C> 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.

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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 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 2,800 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). The construction of mining, milling and infrastructure facilities is estimated to take 18 months to complete. The total capital cost to bring the Al Masane project into production is estimated to be \$81.3 million. This cost includes the pre-production development of the mine, the construction of a 2,000 tonne per day concentrator, infrastructure with a 300 man camp 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 trackless mining equipment using either cut-and-fill or open-stopping methods depending on the shape and location of each orebody. Once the raw ore is mined, it would be subjected to 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. Total output per year is estimated to be 22,000 ounces of gold and 800,000 ounces of silver. 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. The cash flow projection for a base case was made by WGM based on the assumption that 50% of the financing of the project will come from the Saudi Industrial Development Fund, which charges 2.5% service charge, 25% from commercial loans at an interest rate of 5% and 25% from equity financing. The cash flow projection includes the repayment of the \$11 million loan outstanding to the Saudi government in one payment at the end of

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the mine life. Based on these assumptions, and assuming the average prices of metal over the life of the mine to be \$1.00 per pound for copper, \$0.60 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 14% to the project, a rate of return of 11.9% and a net cash flow of \$26.6 million to the equity investors in the new Saudi public stock company, and a net cash flow of \$37 million to the Company. Other cash flow scenarios calculated to show the effect of various opportunities and risks associated with the project were also prepared. Assuming the mine begins commercial production in mid-1996, as contemplated in the feasibility study, the Company would not pay any income tax to the Saudi government for the first five years or until after mid-2001. In the feasibility study, WGM recommends that the Company make a decision to 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.

Project Financing and Mining Lease. Pursuant to the mining lease agreement, after the profitability of the project is established, as determined by the Saudi Arabian government, the Company will form a Saudi public stock company with the Petroleum and Mineral Organization ("Petromin"), the official mining and petroleum company of the Saudi Arabian government. The Company will own 50% of the shares of the Saudi public stock company and Petromin no more than 25% of the shares. The remaining shares will be offered for sale in Saudi Arabia pursuant to a public subscription. In consideration for its receiving shares in the Saudi public stock company, the Company intends to transfer title to the mining lease to the Saudi public stock company, including responsibility for the repayment of the \$11 million loan from the Saudi Arabian government and the other obligations specified in the mining lease. 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 should occur only after assured profits from commercial operations of the mine. The instructions added that Petromin shall have the right to purchase shares in the Saudi public stock company any time it desires.

Pursuant to these instructions the Company retained Carlyle SEAG ("Carlyle"), of Washington, D.C. and Saudi Arabia, as the Company's financial advisor in connection with the Al Masane mining project. Carlyle's services will include, but not be limited to, (1) advising on the capitalization structure of the proposed Saudi company to be established for the project; (2) the raising of capital funds for the project implementation; and (3) assisting the Company on the filing of all licenses and necessary documents for regulatory purposes.

While the Company agreed in the mining lease not to request a loan which would fund 50% of the capital cost of the project from the Saudi Public Development Fund, the Company intends to apply for a similar loan from the Saudi Industrial Development Fund. The Saudi Industrial Development Fund makes interest-free loans to industrial projects in Saudi Arabia and charges a 2.5% service fee. The Company believes that it may be able to finance the 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.

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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 jointly secured by the Company and National Mining from the Saudi Arabian government. The mining lease provides that the Company will repay the loan from the profits of the project. 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 agrees to pay surface rental at the rate of ten thousand Saudi Riyals (approximately \$2,667 at the current exchange rate) per square kilometer per year during the period of the lease. 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 Mining Code, 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 comes first. 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 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 15 of this Report for information concerning the location of the Al Masane project.

Other Exploration Areas in Saudi Arabia

The Company, along with National Mining and another Saudi private company, have also applied to the Saudi government for an exploration license covering a large area in northern Saudi Arabia

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known as Ghurayyah. Preliminary investigations have indicated that the Ghurayyah area contains substantial columbium, tantalum and other mineral deposits.

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 it has applied for certain additional exploration licenses in that country, including the Ghurayyah license.

With respect to the license areas, the Company and National Mining are parties to an agreement with Petromin which governs the rights of the parties if the exploration licenses granted to the Company and National Mining 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 exploration licenses granted to the Company and National Mining. The 25% interest is to be derived from National Mining's interest in the mining lease. The Company will have a 50% interest in the mining lease subject to this arrangement.

U.S. Mineral Interests

The Company has other mineral interests in the United States, including approximately a 55% beneficial, and approximately a 46% direct, equity interest in Pioche-Ely Valley. The Coal Company does not own or hold any mineral interests and is presently inactive. The future of the Coal Company's operations is uncertain. The Refining Company is a party to a joint venture with a Saudi company and the former owners of TOCCO the purpose of which is to engage in the trading of crude petroleum and refined petroleum products. The joint venture has not consummated any petroleum trading transactions.

Petroleum Refinery

South Hampton owns and operates a petroleum refinery near Silsbee, Texas and currently employs 45 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: (1) a pentane-hexane unit; (2) a catalytic reformer; (3) an aromatics hydrotreating and fractionation unit; (4) a cyclopentane unit; (5) an aromax unit; (6) an aldehyde hydrogenation unit; and (7) a specialty fractionation unit. All of these units are presently in operation, except the aldehyde hydrogenation unit. South Hampton is evaluating potential processing alternatives for the aldehyde hydrogenation unit.

The design capacity of the pentane-hexane unit is approximately 2,200 BPD of feedstock. The unit averaged 1,650 barrels per stream day during 1994. 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.

The catalytic reforming unit is a standard industry design using platinum-rhenium catalyst which produces an aromatics concentrate used as feedstock for the 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 standby source of hydrogen for the pentane-hexane unit and does not run continually. The unit operates only when the aromax unit has mechanical difficulties or when feedstock balances dictate. The unit averaged 284 barrels per stream day during 1994.

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 was placed into service for a toll processing customer in mid-1993 and is expected to continue operation at a throughput rate of approximately 110 barrels per stream day.

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 261 barrels per stream day during 1994.

The aromax 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 pentane-hexane unit and the other hydrotreaters. The unit averaged throughput of 211 barrels per stream day during 1994. Chevron Research has agreed to continue development of the aromax process. The unit has continued to successfully operate as designed.

The specialty fractionation unit consists of two fractionation towers and a sulphur treater and has a design capacity of 1,000 BPD. The unit is being used in toll processing for a customer and averaged 495 barrels per stream day during 1994.

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.

The upgrading and expansion projects were completed at a cost which exceeded the capital resources available to South Hampton to finance such activities. Financing for the upgrading and expansion projects was provided from advances by the Company through the Refining Company to South Hampton of a portion of the proceeds of the sale of shares of the Company's Common Stock and the advances by Chevron Research and another customer. The advances by the Company through the Refining Company to South Hampton for the upgrading and expansion of the refinery were \$550,000 in the aggregate, \$510,000 of which amount is secured by a lien on the assets and properties of South Hampton, which is subordinate to the liens securing the indebtedness of South Hampton to Den norske Bank AS.

Gulf States owns and operates three 8" pipelines aggregating approximately 45 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

With the exception of revenues generated by the operations of the Refining Company, the Company has been without significant operating revenues since 1972. Accordingly, it has been necessary for the Company continually to seek additional debt and equity financing in order to have funds to continue development activities. In 1992, the Company sold 105,000 shares of its Common Stock for \$105,000, borrowed \$250,000 from a Saudi Arabian investor which was used as partial payment of the purchase price of 1,500,000 shares of the Company's Common Stock which the Company sold to the investor at \$1.00 per share, borrowed a total of \$75,000 from a stockholder of the Company who is the Vice Chairman of National Mining, which amount was payable on demand, and issued 500,000 shares of its Common Stock, valued by the Company's Board of Directors at \$1.00 per share, in exchange for the cancellation of certain indebtedness owed to this stockholder.

In 1993, the Company (1) sold 75,000 shares of its Common Stock at \$1.00 per share to a private Saudi company controlled by

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a director of the Company and sold an additional 300,000 shares of its Common Stock at \$1.00 per share to the same purchaser pursuant to an option exercise, which shares are partly paid as a result of \$100,000 of the exercise price having been paid during 1993, (2) sold 3,000,000 shares of its Common Stock at \$1.00 per share to a Saudi Arabian investor, \$300,000 of the purchase price of which consisted of the cancellation of various loans made to the Company, (3) sold 256,250 shares of its Common Stock for \$256,250, (4) borrowed \$13,279 from a stockholder of the Company who is the Vice Chairman of National Mining pursuant to an interest-free demand note and (5) issued 200,000 shares of its Common Stock, valued by the Company's Board of Directors at \$1.00 per share, to a company owned by the wife of the President of the Company in exchange for the cancellation of certain indebtedness.

In 1994, the Company (1) negotiated an extension until June 30, 1995 of the maturity of the Amended and Restated Credit Agreement with Den norske Bank AS, (2) issued 14,000 shares of its Common Stock of \$1.00 per share pursuant to an option exercised by the company's Chairman of the Board in exchange for the cancellation of certain indebtedness, (3) consolidated two notes payable by the Company's President and Chief Executive Officer, in the amounts of \$99,000 and \$27,000, which matured on December 31, 1993 and January 31, 1994, respectively, into one note for \$126,000 having a December 31, 1995 maturity date and bearing interest at the rate of six percent per annum, (4) received \$50,000 from a 1993 sale of its Common Stock to a private Saudi company controlled by a director of the Company pursuant to a partial option exercise and (5) offset \$30,000 in unpaid compensation due to the Company's Chairman of the Board against amounts owned to the Company by four companies owned by the Chairman of the Board. 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.

The Refining Company had operating income of approximately \$2,414,000, before depreciation and amortization of \$646,000, on gross refined product sales of \$17,564,000 for the 1994 fiscal year, compared with operating income of approximately \$710,000, before depreciation and amortization of \$678,000, on gross refined product sales of \$15,103,000 for the 1993 fiscal year, and a net operating loss of approximately \$113,000, before depreciation and amortization of \$682,000, on gross refined product sales of \$13,320,000 for the 1992 fiscal year.

Management believes that South Hampton will be able to continue to attain a positive cash flow as a result of the upgrading and expansion projects. Any such cash flow would, however, be insufficient to retire the debt due on June 30, 1995, to Den norske Bank AS. At that time, South Hampton will be required to attempt to re-extend or renegotiate the loan or seek to

obtain additional financing. It is possible that any further extension or renegotiation will not be permitted without the retirement of a significant portion of the debt. Failure to extend or renegotiate the loan with Den norske Bank AS would require the Company to seek alternative sources of financing which, if unsuccessful, could result in a foreclosure action and subsequent loss of the refinery. Expiration of the guarantee of the letter of credit portion of the Amended and Restated Credit Agreement resulted in Den norske Bank AS drawing down a \$1,500,000 letter of credit provided by the guarantor. As a consequence, the Company is indebted to the guarantor for such amount.

In connection with the latest extension of the Den norske Bank AS loan, South Hampton agreed to make quarterly principal payments of \$200,000 and the Company committed to use its best efforts to raise and contribute new equity to South Hampton of at least \$1,500,000 by June 30, 1995, such funds to be used by South Hampton to pay amounts outstanding under the Amended and Restated Credit Agreement.

In addition to requiring that a substantial portion of South Hampton's cash flow be applied to reduce the amount outstanding, the Amended and Restated Credit Agreement with Den norske Bank AS prohibits the payment of dividends by South Hampton. South Hampton is also required to collect all receivables through a cash collateral account at a local bank. Only the amount of funds required to operate South Hampton's business may be used and weekly reports of cash receipts and disbursements in the cash collateral account must be provided to Den norske Bank AS. If South Hampton defaults on the credit agreement, Den norske Bank AS has the right to freeze the funds in the cash collateral account. South Hampton met all of the loan covenants throughout 1994.

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 Coal Company's lack of significant assets, combined with the Company's lack of operating funds, inhibits any future activities of the Coal Company. The Company is planning limited exploration of the Pioche-Ely Valley properties in 1995.

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 feasibility study show the estimated total capital costs of the project to be \$81.3 million.

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.

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, and Mr. Drew Wilson, who works on a part-time basis for the Company and serves as its Secretary and Treasurer. The other employees of the Company, numbering approximately 29, 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 45 persons.

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[map]

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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 and National Mining exclusive mineral exploration licenses to explore and develop the Wadi Qatan area in southwestern Saudi Arabia. The companies were 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 and National Mining have also applied for an additional license covering an area surrounding the original Al Masane prospect, which is referred to as the Greater Al Masane area. Although the license has not been formally granted, the companies have been authorized in writing to carry out exploration work on the area. Reference is made to the map on page 15 of this Report for information concerning the location of the foregoing areas. The Company, together with National Mining and another Saudi private company, the Red Sea Mining Company, have also applied for an exploration license covering the Ghurayyah area in northern Saudi Arabia.

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 and National Mining are parties 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 and National Mining is

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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 and Jebel Harr 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 sulphides 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 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. The Company plans to obtain a renewal of its exploration licenses in the Wadi Qatan and Jebel Harr areas to enable it 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 another 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.

Ghurayyah. In 1980, the Company, together with National Mining Company and the Red Sea Mining Company, applied jointly for an additional exploration license covering the 7,000 square kilometer Ghurayyah area in the northern part of Saudi Arabia. The application is still pending with the Saudi Arabian Ministry of Petroleum and Mineral Resources.

A preliminary investigation of the area, which included core drilling, was arranged by the Saudi Arabian Ministry and conducted by WGM prior to the time the license application was filed. Based on the preliminary investigation, WGM observed in December 1980

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that "[t]he columbium and tantalum content to a depth of 250 meters below the surface could add very significantly to world resources."

Pursuant to an exploration and development contract between the parties, the Company, National Mining and Red Sea would each have a 15% interest in the Ghurayyah license and the responsibility to carry out the exploration work, and Petromin would have a 55% interest. The costs of exploration would be shared based on each participant's percentage interest in the license. As between the parties responsible for the exploration activities, the Company would be the operator on the license area.

Refining Operations

South Hampton owns and operates a petroleum refinery near Silsbee, Texas. South Hampton owns all of the capital stock of Gulf States, which 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 States are more fully described in Item 1. Business.

Nevada Mining Properties

There are 48 patented and 84 unpatented claims totaling approximately 3,700 acres in the Pioche-Ely Valley 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). The Company planned to drill a 1,500 foot test hole in 1994 in search of zinc deposits. Drilling was conducted in September 1994. The drill hole encountered formation problems at 700 feet and further drilling had to be abandoned. A new site will be selected and a second hole is expected to be drilled in 1995.

There is a 300-ton-a-day processing mill on property owned by Pioche-Ely Valley. The mill is not currently in use and a significant expenditure would be required in order to put the mill into continuous operation. Pursuant to a lease commencing on October 1, 1993, the Wide Awake mine property was leased for a primary term of twenty-seven months, which lease will continue as long as minerals are produced in commercial quantities or unless terminated by the parties. The lease stipulates a 6% royalty on net smelter returns with no annual rental required. A significant core hole is planned to be drilled on the Wide Awake claim in mid-1995.

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Colorado Coal Properties

In March 1994, the Mined Land Reclamation Division, Department of Natural Resources, of the State of Colorado elected to exercise its rights under the letter of credit given by the Coal Company to secure completion of the reclamation work on coal properties in Colorado previously leased by the Coal Company. The Coal Company was required by the Mined Land Reclamation Division to monitor the completed reclamation work and conduct additional reclamation work on the coal properties until 2000. The letter of credit was secured by a \$36,000 certificate of deposit and in April 1994 was paid to the State of Colorado. The Mined Land Reclamation Division's action concludes the Coal Company's involvement in the reclamation project. The Coal Company has a tax loss carry-forward of approximately \$14.8 million which is limited to its net income. The Coal Company is currently negotiating with a company toward the possible use of this amount, although there can be no assurance that any agreement relating thereto will be reached.

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 the northern part of 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 filed suit on July 18, 1994 in the 88th Judicial District Court in Hardin County, Texas against National Union Fire Insurance Company arising from the claim of South Hampton under the Uniform Declaratory Judgment Act for a ruling as to the construction of an insurance contract issued by National Union insuring South Hampton. South Hampton also asserted claims against National Union for breach of contract, negligence, breach of the duty of good faith and fair dealing and certain violations of the Texas Insurance Code. This case was removed to the United States District Court on August 22, 1994. The court ordered that it will first consider South Hampton's contractual coverage claims under the Uniform Declaratory Judgment Act and abated all of the other claims pending the outcome of the contractual coverage claims.

Any proceeds received by South Hampton from this cause of action would be payable by South Hampton to Cajun Energy, Inc. and E-Z Mart Stores pursuant to the terms of a judgment entered against South Hampton. South Hampton consented to a settlement agreement with Cajun Energy and E-Z Mart Stores in May 1994 whereby the plaintiffs took a judgment against South Hampton for the amounts claimed and the plaintiffs signed a "non-execution agreement" agreeing not to execute upon the judgment in return for the assignment by South Hampton of certain claims against National Union. This concludes the claims and actions against South Hampton in these matters.

South Hampton, together with over twenty-five other companies, is 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 John Ricklefsen and James Griffin, 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 claim 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 intends to vigorously defend against these lawsuits.

The Company is not involved in any proceeding regarding environmental matters. See Note 4 to the Consolidated Financial Statements for a discussion of certain environmental matters.

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

No matter was submitted to a vote of the Company's stockholders during the fourth quarter of 1994.

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 1994 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, 1994, of the Company's 1994 Annual Report to Stockholders filed herein as Exhibit 13, which portion of such Annual Report is incorporated herein by reference.

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 1994 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 1994 Annual Report to Stockholders filed herein as Exhibit 13, are incorporated herein by reference.

Item 9. Disagreements on Accounting and Financial Disclosure.

None.

PART III

Item 10. Directors and Executive Officers of the Registrant.

This information is set forth under the captions "Nominees for Election as Directors" and "Executive Officers" of the

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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.

PART IV

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

<S> <C> <C>

- (a) 1. The following financial statements are incorporated by reference from the Company's 1994 Annual Report to Stockholders filed herein as Exhibit 13:

Report of Independent Accountants.
Consolidated Balance Sheets dated December 31, 1994 and 1993.
Consolidated Statement of Operations for the three years ended December 31, 1994.
Consolidated Statement of Stockholders' Equity for the three years ended December 31, 1994.
Consolidated Statement of Cash Flows for the three years ended December 31, 1994.
Notes to Consolidated Financial Statements.

2. The following documents, separately bound, 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

</TABLE>

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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) Form of Contract for the Exploration and Development of the Al-Ghurayyah Area entered into in December 1982 between Petromin and the Company, National Mining Company and Red Sea Mining Company (incorporated by reference to Exhibit 10(c) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).

- 10(d) 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(e) 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)).

</TABLE>

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- <S> <C>
- 10(f) 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(g) 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(h) Amended and Restated Credit Agreement dated December 13, 1990 between South Hampton Refining Company and Den norske Bank AS, together with related Promissory Note, Cash Collateral Account Agreement, Subordination Agreement and Intercreditor Agreement, all of even date therewith (incorporated by reference to Exhibit 10(h) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
- 10(i) Second Lien Promissory Note dated July 28, 1989 from South Hampton Refining Company to American Shield Refining Company (incorporated by reference to Exhibit 10(i) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
- 10(j) Subordination Agreement dated July 28, 1989 by and among Texas Oil and Chemical Co. II, Inc., South Hampton Refining Company, Gulf States Pipe Line Company, the Company, American Shield Refining Company and den Norske Creditbank (incorporated by reference to Exhibit 10(j) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
- 10(k) Amendment No. 1 and Amendment No. 2 to Amended and Restated Credit Agreement dated March 15, 1991 and December 31, 1991, respectively, between South Hampton Refining Company and Den norske Bank AS, together with related Guaranty dated as of December 31, 1991, by Texas Oil & Chemical Co. II, Inc. in favor of Den norske Bank AS, Pledge Agreement and Irrevocable Proxy dated as of December 31, 1991, between Texas Oil &

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- <S> <C>
- Chemical Co. II, Inc. and Den norske Bank AS and Pledge Agreement and Irrevocable Proxy dated as of December 31, 1991, between South Hampton Refining Company and Den norske Bank AS (incorporated by reference to Exhibit 10(k) 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 February 28, 1994 by and between South Hampton Refining Company and Den norske Bank AS (incorporated by reference to Exhibit 10(l) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
- 10(m) Letter Agreement dated June 2, 1994 by and between South Hampton Refining Company and Den norske Bank AS together with related Letter Agreement dated June 2, 1994 by and between the Company and Den norske Bank AS (incorporated by reference to Exhibit 10(m) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
- 10(n) Letter Agreement dated December 2, 1994 by and between South Hampton Refining Company and Den norske Bank AS (incorporated by reference to Exhibit 10(n) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
- 10(o) 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(p) Addendum to the Agreement Relating to AROMAX 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

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Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).

10(q) 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(r) Agreement for Purchase of Feedstock dated July 1, 1992 by Silsbee Trading and Transportation Corp. and South Hampton Refining Company (incorporated by reference to Exhibit 10(r) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).

10(s) One-Year Adjustable Interest Rate Note dated February 1, 1995, effective December 31, 1994, from Texas Oil & Chemical Co. II, Inc. to Silsbee State Bank, together with Deed of Trust of even date therewith (incorporated by reference to Exhibit 10(s) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).

10(t) 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(u) 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(v) Lease Agreement dated as of August 13, 1993 by and among Pioche-Ely Valley Mines, Inc., Minerals Processing, Inc. and World Hydrocarbons, Inc. (incorporated by reference to Exhibit 10(v) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).

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10(w) Letter Agreement dated March 27, 1995 between Carlyle (SEAG) and the Company.

13 1994 Annual Report to Stockholders. With the exception of the information incorporated by reference into Items 5,6,7,8 and 14 of this Form 10-K, the 1994 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.

</TABLE>

(b) No reports on Form 8-K were filed during the last quarter of the period covered by this Report.

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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 27, 1995

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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 27, 1995.

<TABLE>
 <CAPTION>
 Signature

Title

| | |
|---|--|
| ----- <S> /s/ Hatem El-Khalidi ----- Hatem El-Khalidi | <C> President, Chief Executive Officer and Director (principal executive officer) |
|---|--|

| | |
|---|--|
| /s/ Drew Wilson ----- Drew Wilson | Secretary and Treasurer (principal financial and accounting officer) |
|---|--|

| | |
|---|---------------------------------------|
| /s/ John A. Crichton ----- John A. Crichton | Chairman of the Board and Director |
|---|---------------------------------------|

| | |
|--|----------|
| /s/ O.W. Hammonds ----- Oliver W. Hammonds | Director |
|--|----------|

| | |
|----------------------------|----------|
| _____ Harb S. Al Zuhair | Director |
|----------------------------|----------|

| | |
|---|----------|
| /s/ Mohammed O. Al-Omar ----- Mohammed O. Al-Omar | Director |
|---|----------|

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EXHIBIT INDEX

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| <u><S></u> | <u><C></u> |
| 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)). |
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| 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) | Form of Contract for the Exploration and Development of the Al-Ghurayyah Area entered into in December 1982 between Petromin and the Company, National Mining Company and Red Sea Mining Company (incorporated by reference to Exhibit 10(c) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)). |

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10(k) Amendment No. 1 and Amendment No. 2 to Amended and Restated Credit Agreement dated March 15, 1991 and December 31, 1991, respectively, between South Hampton Refining Company and Den norske Bank AS, together with related Guaranty dated as of December 31, 1991, by Texas Oil & Chemical Co. II, Inc. in favor of Den norske Bank AS, Pledge Agreement and Irrevocable Proxy dated as of December 31, 1991, between Texas Oil & Chemical Co. II, Inc. and Den norske Bank AS and Pledge Agreement and Irrevocable Proxy dated as of December 31, 1991, between South Hampton Refining Company and Den norske Bank AS (incorporated by reference to Exhibit 10(k) 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 February 28, 1994 by and between South Hampton Refining Company and Den norske Bank AS (incorporated by reference to Exhibit 10(l) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).

10(m) Letter Agreement dated June 2, 1994 by and between South Hampton Refining Company and Den norske Bank AS, together with related Letter Agreement dated June 2, 1994 by and between the Company and Den norske Bank AS (incorporated by reference to Exhibit 10(m) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).

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10(n) Letter Agreement dated December 2, 1994 by and between South Hampton Refining Company and Den norske Bank AS (incorporated by reference to Exhibit 10(n) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).

10(o) 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(p) Addendum to the Agreement Relating to AROMAX 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(q) 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(r) Agreement for Purchase of Feedstock dated July 1, 1992 by Silsbee Trading and Transportation Corp. and South Hampton Refining Company (incorporated by reference to Exhibit 10(r) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).

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- 10(s) One-Year Adjustable Interest Rate Note dated February 1, 1995, effective December 31, 1994, from Texas Oil & Chemical Co. II, Inc. to Silsbee State Bank, together with Deed of Trust of even date therewith (incorporated by reference to Exhibit 10(s) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
- 10(t) 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(u) 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(v) Lease Agreement dated as of August 13, 1993 by and among Pioche-Ely Valley Mines, Inc., Minerals Processing, Inc. and World Hydrocarbons, Inc. (incorporated by reference to Exhibit 10(v) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
- 10(w) Letter Agreement dated March 27, 1995 between Carlyle (SEAG) and the Company.
- 13 1994 Annual Report to Stockholders. With the exception of the information incorporated by reference into Items 5, 6, 7, 8 and 14 of this Form 10-K, the 1994 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.

</TABLE>

EXHIBIT 10(w)

Letter of Agreement

This Letter of Agreement is made this 27th day of March, 1995 by and between Carlyle SEAG ("SEAG") and Arabian Shield Development Company ("ASDC").

WHEREAS this Letter of Agreement sets forth that ASDC wishes to enter into a contractual arrangement retaining SEAG as its financial advisor in connection with the financing of the Al Masane Mining Project ("the Project"); and

WHEREAS SEAG is currently disposed to provide certain financial advisor services;

THEREFORE, it is agreed that the scope of the services to be provided by SEAG will include, but is not limited to, (1) advising on the capitalization structure (SIDF, Commercial Debt and Equity) of the newly established Saudi company "Newco", established for the Project; (2) raising of capital for project implementation and (3) assisting ASDC in the filing of all licenses and needed documents for regulatory purposes.

It is further agreed that ASDC shall prepare or cause to be prepared necessary loan documentation and supporting information including a full feasibility study, or as agreed by SEAG, ASDC shall provide SEAG all necessary assistance in the accomplishment of the same.

Accordingly, SEAG will receive the following compensation for services rendered in its role as financial advisor.

1. SEAG will receive a retainer payment of two hundred and fifty thousand US dollars (\$250,000), to cover a period of one year in duration, seventy five thousand dollars (\$75,000) of which is payable by ASDC upon the signing of this Agreement, and twenty five thousand (\$25,000) monthly thereafter. In no case or circumstances shall SEAG receive a retainer payment of less than one hundred twenty five thousand US Dollars (\$125,000).
2. SEAG will receive cash compensation equaling two and one quarter percent (2 1/4%) of the total capital value, inclusive of debt and equity funding, of the Al Masane Project in recognition of SEAG's role in the financial structuring of the Project and in providing financial and such other assistance as may be provided.
3. SEAG will also receive a cash compensation fee totaling five percent (5%) of the amount of equity funds raised from equity investors up to US twenty five million (\$25,000,000); an additional cash compensation fee totaling three percent (3%) for equity funds raised from investors between US twenty five million (\$25,000,000) and US fifty million (\$50,000,000); an additional cash compensation fee totaling two percent (2%) for equity funds raised from investors between US fifty million (\$50,000,000) and US seventy five million (\$75,000,000); an additional cash compensation fee totaling one percent (1%) for equity funds raised from investors equal to or above US seventy five million (\$75,000,000).
4. In addition SEAG shall also be entitled to receive compensation in the form of an option to purchase two million shares (2,000,000), or approximately 10%, of ASDC's common stock, during a period of five (5) years, commencing upon the first closing of either the debt or equity portion of the financing for the Al Masane Project, at an exercise price of US one dollar (\$1) per share. Such issuance will be made in compliance with Rule 144 of the SEC. It is understood that standard anti-dilution provision will be in effect for the full period of the option.
5. SEAG shall nominate one member of the Board of Directors in its next annual meeting of the shareholders to be held on May 9, 1995. SEAG shall nominate a second Board member upon the closing of the financing for the Al Masane Project.
6. SEAG reserves the right and at its sole discretion to withdraw from this Agreement, and will give ASDC one month's notice prior to its withdrawal, if SEAG determines that the transaction is no longer reasonably viable based on due diligence findings; availability of financing, especially SIDF funding and/or otherwise adverse material changes. In such event SEAG shall not be

entitled to any compensation pursuant to paragraphs 2,3 and 4 herein. ASDC also reserves the right and at its sole discretion to withdraw from this agreement if there is a determination of fraud or gross negligence on the part of SEAG in its performance relating to the Project.

7. ASDC agrees to defend, indemnify and hold harmless (including, without limitations, reasonable attorney fees and expenses) SEAG and SEAG affiliates, each of the employees, directors, officers, stockholders and agents of SEAG, and their respective successors, against any and all losses, damages, deficiencies or liabilities are caused by, resulting or arising from or otherwise relating to the Project, unless such losses, damages, deficiencies or liabilities are caused by, resulting or arising from fraud or gross negligence by SEAG in its performance relating to the Project.

8. It is agreed that SEAG shall be reimbursed for all of its reasonable out of pocket expenses with regard to its role as financial advisor in the financing of the Al Masane Project. If such expenses are expected to exceed US ten thousand dollars (\$10,000) in any given month, an estimate for such month shall be prepared and presented to ASDC for approval, and prompt approval shall not be unreasonably denied by ASDC. ASDC will be responsible for reimbursing SEAG's expenses within five (5) business days following the receipt of such expenses, SEAG will instruct in writing ASDC as to the banking institution and appropriate account which the reimbursement should be deposited.

9. The duly authorized parties designated below hereby signify their agreement with the terms and conditions contained herein through execution of this letter of agreement by signing as indicated below,

Carlyle SEAG

By: /s/ AMB. ALTON G. KEEL JR.
Name: Amb. Alton G. Keel Jr.
Title: Chairman

Arabian Shield Development Company

By: /s/ HATEM EL-KHALIDI
Name: Hatem El-Khalidi
Title: President

ARABIAN SHIELD
Development Company

Annual Report to Stockholders
For The Year Ended December 31, 1994

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 of Toronto, Canada ("WGM") to update the feasibility study for that area. 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. Under the terms of the mining lease agreement, the Company will pay rental 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 during the period of the lease for the total lease area of 44 square kilometers. The Company will also pay the Saudi 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.

Pursuant to the terms of the mining lease agreement, the Company undertakes to repay the \$11 million loan provided to the Company and National Mining Company in 1979 by the Ministry of Finance and National Economy, in accordance with the terms of an agreement to be reached 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.

The mining lease agreement also provides that, after the profitability of the project is established, as determined by the Saudi Arabian government, the Company will form a Saudi public stock company with the Petroleum and Mineral Organization ("Petromin"), a company wholly-owned by the Saudi government. The Company will own 50% of the shares of the Saudi public stock company and Petromin no more than 25% of the shares. The remaining shares will be offered for sale in Saudi Arabia pursuant to a public subscription. In consideration for its receiving shares in the Saudi public stock company, the Company will transfer title to the mining lease to the Saudi public stock company, including responsibility for the repayment of the \$11 million loan from the Saudi Arabian government and the other obligations under the mining lease. 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 should occur only after assured 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.

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 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

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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.

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 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 2,800 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). The construction of mining, milling and infrastructure facilities is estimated to take 18 months to complete. The total capital cost to bring the Al Masane project into production is estimated to be \$81.3 million. This cost includes the pre-production development of the mine, the construction of a 2,000 tonne per day concentrator, infrastructure with a 300 man camp 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 trackless mining equipment using either cut-and-fill or open-stopping methods depending on the shape and location of each orebody. Once the raw ore is mined, it would be subjected to 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. Total output per year is estimated to be

22,000 ounces of gold and 800,000 ounces of silver. After smelter refining process, the metals could be sold by the Company or the smelter for the Company's account in the open market.

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WGM prepared an economic analysis of the project utilizing cash flow projections. The cash flow projection for a base case was made by WGM based on the assumption that 50% of the financing of the project will come from the Saudi Industrial Development Fund, which charges 2.5% service charge, 25% from commercial loans at an interest rate of 5% and 25% from equity financing. The cash flow projection includes the repayment of the \$11 million loan outstanding to the Saudi government in one payment at the end of the mine life. Based on these assumptions, and assuming the average prices of metal over the life of the mine to be \$1.00 per pound for copper, \$0.60 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 14% to the project, a rate of return of 11.9% and net cash flow of \$26.6 million to the equity investors in the new Saudi public stock company, and a net cash flow of \$37 million to the Company. Other cash flow scenarios calculated to show the effect of various opportunities and risks associated with the project were also prepared. Assuming the mine begins commercial production in mid-1996, as contemplated in the feasibility study, the Company would not pay any income tax to the Saudi government for the first five years or until after mid-2001. In the feasibility study WGM recommends that the Company make a decision to 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.

On March 27, 1995 the Company's Board of Directors approved a Letter of Agreement between the Company and Carlyle SEAG ("Carlyle"), of Washington, D.C. and Saudi Arabia, whereby Carlyle has been retained as the Company's financial advisor in connection with the Al Masane mining project. Carlyle's services will include, but not be limited to, (1) advising on the capitalization structure of the proposed Saudi company to be established for the project; (2) the raising of capital funds for the project implementation; and (3) assisting the Company in the filing of all licenses and necessary documents for regulatory purposes. In addition to compensation for their services, including the grant of a five (5) year option allowing Carlyle to purchase 2,000,000 shares of the Company's Common Stock at \$1.00 per share, the agreement provides that Carlyle is entitled to nominate one person for election to the Company's Board of Directors. As a result, at the next meeting of the Board of Directors the directors will appoint the Carlyle nominee to the Board of Directors to serve until the next annual meeting of the stockholders. Carlyle is also entitled to nominate another person for election to the Company's Board of Directors upon the closing of the financing for the Al Masane project.

The Company owns, through a wholly-owned subsidiary, South Hampton Refining Company, of Silsbee, Texas ("South Hampton"), which owns and operates a petrochemical plant which produces pure pentanes and hexanes and other specialty chemicals for the plastics industry. Total revenues for 1994 for the refinery were \$17.7 million and the cash flow realized was approximately \$2.4 million. It is significant that the plant sells about 40% of all pentanes consumed in the United States.

In May 1994, a lawsuit against South Hampton Refining Company relating to the manufacture and sale of allegedly defective gasoline went to trial and judgment was entered against South Hampton. In consideration of the judgment, another lawsuit involving the same parties and identical issues was dismissed. At the trial, South Hampton consented to a settlement agreement whereby the plaintiffs took a judgment against South Hampton for the amounts claimed and the plaintiffs signed a "non-execution agreement" agreeing not to execute upon the judgment in return for the assignment by South Hampton of certain claims against its insurance carrier. This concludes the claims and actions against South Hampton in these matters.

The Company has had discussions with Chevron Chemical Company regarding the Company's proposal to purchase 5,000 barrels per day of mixed pentanes from an Aromax petrochemical project to be built in

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Jubail, Saudi Arabia by Chevron Chemical in joint venture with Saudi Venture Capital Group (SVCS). The Company and some Saudi joint venture partners, all of whom are directors and/or stockholders of the Company, contemplate building a processing plant located next to the Aromax plant in Saudi Arabia. As proposed, the Company would have a 25% interest in the joint venture. Chevron Chemical advised the Company by letter that Chevron Chemical and SVCS have jointly agreed to commit to supply the joint venture's proposed pentane project with up to 5,000 barrels per day of mixed pentane feedstock. Engineering and marketing studies of the project have been made by outside consultants which reflect positive results. Planning has begun toward the construction and operation of the Aromax plant and the joint venture's processing plant. Construction is estimated to be completed in late 1996. The Company will begin applying to the Saudi government for a license for the project when the Aromax project receives final approval from the Saudi government.

The Company directly owns approximately 46% and beneficially owns approximately 55% of the outstanding capital stock of Pioche-Ely Valley Mines, Inc. ("Pioche-Ely Valley"), an inactive mining company. Pioche-Ely Valley's principal assets are a 300 ton per day mill, and 48 patented and 84 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.

Based on geophysical work of the mining claims of Pioche-Ely Valley in 1989 by a major mining company, the Company planned to drill a 1,500 foot test hole in 1994 in search of zinc deposits. Drilling was conducted in September 1994. The drill hole encountered formation problems at 700 feet and further drilling had to be abandoned. A new site will be selected and a second hole is expected to be drilled in 1995. One of the mine properties has been leased to a group of investors who plan to begin development operations in 1995. A significant core hole is planned to be drilled on the Wide Awake claim in mid-1995.

Respectfully submitted,

John A. Crichton
Chairman of the Board

Hatem El-Khalidi
President and Chief
Executive Officer

March 27, 1995

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THE COMPANY.

Arabian Shield Development Company (the "Company") was organized as a Delaware corporation in 1967 and is principally engaged in the business of developing its undeveloped mineral properties. None of the undeveloped mineral properties are currently producing and significant capital expenditures will be necessary before any commercial operations are commenced. The Company has operations in both the United States and Saudi Arabia. The Company is primarily engaged in the exploration and development of minerals 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 a bankable feasibility study conducted by an independent mineral consulting firm in 1994 indicate that the proposed Al Masane mining operation is economically viable and has the potential to provide a satisfactory return on investment.

The Company jointly holds with National Mining Company, a private Saudi company, exploration licenses for the Wadi Qatan and Jebel Harr areas in Saudi Arabia. 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 is planning to apply for formal extensions of these licenses in 1995.

The Company has had discussions with Chevron Chemical Company regarding the Company's proposal to purchase 5,000 barrels per day of mixed pentanes from an Aromax petrochemical project to be built in Jubail, Saudi Arabia by Chevron Chemical in joint venture with Saudi Venture Capital Group (SVCS). The Company and some Saudi joint venture partners, all of whom are directors and/or stockholders of the Company, contemplate building a processing plant located next to the Aromax plant in Saudi Arabia. Chevron Chemical advised the Company by letter that Chevron Chemical and SVCS have jointly agreed to commit to supply the Joint Venture's proposed pentane project with up to 5,000 barrels per day of mixed pentane feedstock. As proposed, the Company would have a 25% interest in the joint venture. Engineering and marketing studies of the project have been made by outside consultants which reflect positive results. Planning has begun toward the construction and operation of the Aromax plant and the joint venture's processing plant. Construction is estimated to be completed in late 1996. The Company will begin applying to the Saudi government for a license for the project when the Aromax project receives final approval from the Saudi government.

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 designs for a state of the art zinc refinery. Sherritt's zinc pressure leach technology provides significant advantages over the other existing zinc production processes, including having the reputation as the most favored technology for environmental considerations. In the study Sherritt concludes, after considering all of the presently identifiable elements, that these elements offer a strong potential for the project and enhance the concept. Sherritt encourages the Company to carry out further studies toward the implementation of the project.

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

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An indirect wholly-owned subsidiary of the Company owns and operates a petroleum refinery near Silsbee, Texas. 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 own or hold any mineral interests and is presently inactive. The coal company has a tax loss carry-forwards of \$14.8 million and is currently negotiating with a company toward the possible use of this amount, although there can be no assurance that any agreement relating thereto will be reached.

The Company beneficially owns approximately 55% and directly owns approximately 46% of the outstanding capital stock of a company which leases mineral properties containing 132 inactive mining claims totalling approximately 3,700 acres in southeastern Nevada. There are prospects and mines on these claims which formerly produced silver, gold, lead, zinc and copper.

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 1994 and 1993, respectively, as reported by NASDAQ.

<TABLE>
<CAPTION>

| | 1994 | | | | 1993 | | | |
|-------------|-------|-------|-------|-------|-------|-------|-------|-------|
| | 1st | 2nd | 3rd | 4th | 1st | 2nd | 3rd | 4th |
| <S> High | 2 3/4 | 2 3/8 | 2 1/2 | 2 1/4 | 2 7/8 | 5 3/8 | 4 1/8 | 2 7/8 |
| Low | 2 | 1 3/4 | 1 1/4 | 1 1/2 | 2 1/4 | 2 1/8 | 2 1/4 | 2 1/8 |

At March 20, 1995, there were 979 record holders of the Company's Common Stock. The Company has not paid a dividend since its inception.

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>

| | 1994 | 1993 | 1992 | 1991 | 1990 |
|---|-----------|------------|------------|-----------|------------|
| <S> Revenues..... | \$ 17,765 | \$ 15,267 | \$ 13,468 | \$ 18,707 | \$ 19,173 |
| Net Income (Loss)..... | \$ 2,852 | \$ (1,338) | \$ (2,196) | \$ 452 | \$ (2,880) |
| Net Income (Loss) Per Share..... | \$.14 | \$ (.08) | \$ (.14) | \$.03 | \$ (.19) |
| Total Assets (At December 31)..... | \$ 41,057 | \$ 41,090 | \$ 38,729 | \$ 27,603 | \$ 28,224 |
| Total Long-Term Obligations> (At December 31)..... | \$ 1,148 | \$ 908 | \$ 889 | \$ 1,841 | \$ 1,427 |

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

With the exception of revenues generated by the operations of American Shield Refining Company, a wholly-owned subsidiary of the Company (the "Refining Company"), the Company has been without any significant operating revenues since 1972. Accordingly, it has financed its development activities and its general and administrative costs through the sale of shares of its Common Stock and loans. 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 properties.

During 1994, the Company took certain actions designed to generate additional equity capital and improve its financial condition, including: (1) the negotiation by South Hampton Refining Company, an indirect wholly-owned subsidiary of the Company ("South Hampton"), of an extension until June 30, 1995 of the maturity of the Amended and Restated Credit Agreement with Den norske Bank AS, (2) issued 14,000 shares of its Common Stock at \$1.00 per share pursuant to an option exercise by the Company's Chairman of the Board in exchange for the cancellation of certain indebtedness, (3) consolidated two notes payable by the Company's President and Chief Executive Officer, in the amounts of \$99,000 and \$27,000, which matured on December 31, 1993 and January 31, 1994, respectively, into one note for \$126,000 having a December 31, 1995 maturity date and bearing interest at the rate of six percent per annum, (4)

received \$50,000 from a 1993 sale of shares of its Common Stock to a private Saudi company controlled by a director of the Company pursuant to a partial option exercise and (5) offset \$30,000 in unpaid compensation due to the Company's Chairman of the Board against amounts owed to the Company by four companies owned by the Chairman of the Board.

The exploration licenses jointly held by the Company and National Mining Company for the Wadi Qatan and Jebel Harr areas in Saudi Arabia, by their terms, have expired, although officials of the Saudi 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, 1994 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.

The feasibility study shows the estimated total capital cost to bring the Al Masane project into production to be \$81.3 million. The Company does not have sufficient funds to bring the project into production. Pursuant to the mining lease agreement, after the profitability of the project is established, as determined by the Saudi Arabian government, the Company will form a Saudi public stock company with the Petroleum and Mineral Organization ("Petromin"), the official mining and petroleum company of the Saudi Arabian government. The Company will own 50% of the shares of the Saudi public stock company and Petromin no more than 25% of the shares. The remaining shares will be offered for sale in Saudi Arabia pursuant to a public subscription. In consideration for its receiving shares in the Saudi public stock company, the Company intends to transfer title to the mining lease to the Saudi public stock company, including responsibility for the repayment of the \$11 million loan from the Saudi Arabian government and the other obligations specified in the mining lease. 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 should occur only after assured profits from commercial operations of the mine. The

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instructions added that Petromin will still have the right to purchase shares in the Saudi public stock company any time it desires.

Pursuant to these instructions, the Company retained Carlyle SEAG ("Carlyle") as the Company's financial advisor in connection with the Al Masane mining project. Carlyle's services will include, but not be limited to, (i) advising on the capitalization structure of the proposed Saudi company to be established for the project; (2) the raising of capital funds for the project implementation; and (3) assisting the Company in the filing of all licenses and necessary documents for regulatory purposes.

While the Company agreed in the mining lease not to request a loan which would fund 50% of the capital cost of the project from the Saudi Public Development Fund, the Company intends to apply for a similar loan from the Saudi Industrial Development Fund. The Saudi Industrial Development Fund makes interest-free loans to industrial projects in Saudi Arabia and charges a 2.5% service fee. The Company believes that it may be able to finance the 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 December 31, 1994, the outstanding principal amount under the Amended and Restated Credit Agreement with Den norske Bank AS was \$2,916,951. The entire balance under the Amended and Restated Credit Agreement facility, including amounts drawn under the letter of credit facility, was due on December 15, 1994. The amounts due to Den norske Bank AS were not paid in full on the December 15, 1994 maturity date. The maturity date under the Amended and Restated Credit Agreement has been extended to June 30, 1995. In connection with the latest extension of the Den norske Bank AS loan, South Hampton has agreed to make quarterly principal payments of \$200,000, and the Company committed to use its best efforts to raise and contribute new equity to South Hampton of at least \$1,500,000 by June 30, 1995, such funds to be used by South Hampton to pay

amounts outstanding under the Amended and Restated Credit Agreement.

The Amended and Restated Credit Agreement is secured by all of the assets of South Hampton and all of the issued and outstanding shares of Texas Oil and Chemical Co. II, Inc. ("TOCCO"), South Hampton and Gulf States Pipe Company, Inc. ("Gulf States"), all of which are indirect wholly-owned subsidiaries of the Company. In addition to requiring that a substantial part of South Hampton's cash flow be applied to reduce the amount outstanding, the Amended and Restated Credit Agreement prohibits the payment of dividends by South Hampton. South Hampton is also required to collect all receivables through a cash collateral account at a local bank. Only the amount of funds required to operate South Hampton's business may be used and weekly reports of cash receipts and disbursements in the cash collateral account must be provided to Den norske Bank AS. If South Hampton defaults on the credit agreement, Den norske Bank AS has the right to freeze the funds in the cash collateral account. South Hampton met all of the loan covenants throughout 1994. The Refining Company agreed to subordinate all intercompany notes to the Amended and Restated Credit Agreement. The letter of credit facility was guaranteed by a stockholder of the Company. When this guarantee was not renewed, Den norske Bank AS drew down on the \$1,500,000 letter of credit provided by the stockholder as its guarantee. As a consequence, South Hampton is now indebted to the stockholder for such amount.

The outstanding loan balance exceeded the amount available under the borrowing base ratio, as defined in the Amended and Restated Credit Agreement, until May 1994. South Hampton expects that its outstanding loan balance will be in excess of the amount allowed by the borrowing base ratio from time to time during 1995. South Hampton does not have adequate resources to pay the full amount outstanding under the Amended and Restated Credit Agreement at maturity on June 30, 1995 (or earlier if accelerated due to default). Management believes that South Hampton will continue to make interest payments and monthly reductions on the outstanding principal of this loan as required under the Amended and Restated Credit Agreement.

The advances totalling \$1,363,000 made by the Company through the Refining Company to South Hampton for various refinery upgrading and expansion projects are evidenced by a promissory note bearing interest at a varying rate equal to the interest rate under the Amended and Restated Credit

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Agreement with Den norske Bank AS for as long as any indebtedness remains outstanding thereunder and thereafter at the rate of 2% above the prime commercial rate of NationsBank of Texas, National Association as announced from time to time. The promissory note is secured by a lien on all the physical assets of South Hampton and Gulf States which is subordinate to the lien of Den norske Bank AS under the Amended and Restated Credit Agreement. The note is payable in monthly installments in an amount equal to the monthly cash flow of South Hampton in excess of \$125,000, not to exceed \$25,000 per month, and was due in full on July 28, 1994. An extension of the note is expected to be made in 1995. Repayments of these advances is prohibited under the Amended and Restated Credit Agreement since South Hampton is in default in its loan repayments thereunder.

Although the refinery had net income during 1994, the refinery's historical operations do not demonstrate adequate cash flow to repay the current portion of its debt obligations. The refinery had cash flow from operations in 1994 of approximately \$2.4 million. Den norske Bank AS has indicated that, if certain conditions are met by June 30, 1995, the bank may consider converting a large portion of the indebtedness to a long-term liability, although there are no assurances that any such conversion will occur. Assuming South Hampton is able to renegotiate an extension of the Amended and Restated Credit Agreement with Den norske Bank AS, management believes that the remaining debt obligations can be repaid from increased cash flows from the refinery, but acknowledges that there can be no assurance that such increased cash flows will occur.

If South Hampton is unable to meet its cash needs for debt service from internally generated funds, it may be necessary for management of the Company to re-extend or negotiate its debt obligations or attempt to obtain funds to repay such obligations from the sale of additional Common Stock or through the sale of all or a portion of its interest in South Hampton. There are no assurances that such an extension or renegotiation could be obtained, that such sales could be arranged or that sufficient additional equity financing could be obtained.

The Clean Air Act Amendments of 1990 have had a positive effect on South Hampton'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 South Hampton's product line. Management believes that South Hampton'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 South Hampton continues to manufacture C6 solvents, its manufacturing of these solvents is being phased out. The AROMAX unit, which was jointly developed by South Hampton and Chevron Research, has the ability to convert C6 hydrocarbons into benzene and other more valuable aromatic compounds, which was part of the reason South Hampton participated in the AROMAX 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 attributable to its indirect wholly-owned subsidiary, South Hampton, 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 primarily through sales of its Common Stock and loans, but there is no assurance that sufficient funds can be obtained. The Company currently has in its treasury approximately \$250,000 from which funds are being used for the implementation plan for the Al Masane project and for meeting all of the Company's current expenditures in the United States and Saudi Arabia. This amount should be sufficient until mid-1995 when additional financing will be necessary. In the event that the Company is unable to complete these sales of its Common Stock, obtain additional financing or reach a final agreement on the repayment of the \$11,000,000 loan from the Saudi Arabian government, there is substantial doubt about the Company's ability to continue as a going concern past mid-1995. The Company's financial statements do not include any adjustments that might result from the outcome of these uncertainties.

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The Company adopted Statement of Financial Accounting Standards No. 109, "Accounting for Income Taxes" ("SFAS No. 109") in 1993. SFAS No. 109 requires the Company to compute deferred income taxes based on the amount of taxes payable in future years, after considering changes in tax rates and other statutory provisions that will be in effect in those years. The provision for income taxes includes taxes currently payable and those deferred because of temporary differences between the financial statement and tax bases of assets and liabilities. The adoption had no significant impact on current period earnings or cash flow.

RESULTS OF OPERATIONS

COMPARISON OF THE YEARS 1994 TO 1993

During the fiscal year ended December 31, 1994, the Company had net income of \$2,852,306 compared to a net loss of \$1,338,321 for the fiscal year ended December 31, 1993.

The gross refined product sales in 1994 of \$17,564,226 was an increase of \$2,460,804 from 1993 while the cost of sales in 1994 of \$13,750,750 was an increase of \$436,323 from 1993, resulting in a net margin increase in 1994 of \$2,024,481. There is no assurance that the Refining Company can achieve the same results in 1995. After processing fee income, general and administrative expenses and depreciation and amortization, the operating income of the Company in 1994 of \$2,305,626 was \$3,240,193 more than the operating loss in 1993 of \$934,567. The net income for the refining operations in 1994 of \$3,271,625 was \$3,627,740 more than the net loss in 1993 of \$356,115. Operating income for 1994 included \$975,000 relating to the reversal of a charge in 1992 for potential expenses relating to litigation that was settled in 1994. The extraordinary item of \$578,150 in 1994 was attributed to the settlement of indebtedness owed to a vendor.

The Refining Company's net profit in 1994 reflected the growth in the U.S. economy which began to effect the plastics industry in the last half of 1993. During mid-year 1993, product sales volumes began to strengthen due to increased activity in the industries served by the Refining Company. The number of

customers served by the Refining Company grew slightly during 1994, however the total volume of products sold increased by 15% from 18.6 million gallons in 1993 to 21.4 million gallons in 1994. This was in addition to the 22% increase during 1993. The Refining Company continued the past trend of placing the majority of its production into the higher priced premium petroleum solvent markets. During the last six years the Refining Company has raised the percentage sold into these markets from 53% in 1989 to over 70% for the last four years. The ability to produce products of the quality sufficient for these higher priced markets has enabled the Refining Company to remain competitive even during the down periods in the industry.

The weak economy in 1992 and early 1993 contributed to a lack of toll processing opportunities. 1994 toll processing revenues were \$297,757, an increase of \$133,779, or 82%, over 1993 toll processing revenues. Many in the industry have turned their focus toward complying with federal and state regulations and are not actively searching for new opportunities which would require toll processing services. This is typical of the industry during difficult times and will improve as the economy improves, although there can be no assurance to that effect. The Refining Company has experienced an increase in the number of inquiries relating to toll processing opportunities.

Margins were not good for much of the year 1992 and the early part of 1993. The Clean Air Act has upset the traditional price and supply relationships of many materials in the petroleum world. The spot price of natural gasoline, the primary feedstock for the refinery has in the past normally fluctuated in a range of \$.08 to \$.18 per gallon below the spot price of regular unleaded gasoline. Price fluctuations in the past have depended upon the season of the year and the demand from other parts of the petrochemical industry which also might use natural gasoline for feedstock to various operations. In 1992, the demand from other segments of the petrochemical industry kept the price near the low end of the range much of the year. Demand was strong because more traditional alternative feedstocks for the industry were more scarce and higher priced due to changes brought about in the nationwide gasoline blending pool by the Clean Air Act. It is anticipated that the price relationships in the petroleum products markets will continue

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to find their economic levels, although there can be no assurance to that effect. During the last half of 1993, due to the oversupply of crude oil and a stable demand, the prices of all petroleum prices dropped by as much as 25% from their 1992 levels. The price of natural gasoline also dropped and the Refining Company enjoyed margins which are greater than those experienced during the previous 18 months. The favorable feedstock prices continued throughout most of 1994 and began rising slightly toward the end of the year.

General and administrative expenses decreased by \$172,122 to \$2,036,470 in 1994 from \$2,208,592 in 1993. 1993 expenses included the recording of \$478,500 for the value of stock options granted. Without this 1993 expense, the general and administrative expenses in 1994 would have reflected an increase of \$306,378. This increase was incurred primarily at the refinery and was mostly attributable to higher payroll, insurance and regulatory expenses. The expenses of regulatory compliance and reporting continue to increase. Interest expense, which is practically all attributable to the debt of the refinery, decreased by \$228,974 from \$576,338 in 1993 to \$347,364 in 1994. This decrease in interest expense was attributable to the reversal of an adjustment made in 1993 for accrued interest of \$155,525 on a note which was settled in 1994. Under the terms of the settlement, all accrued interest was forgiven. In 1994, there was a reduced amount of debt. The income tax expense of \$39,973 reflects the federal income tax provision on the Company's net income after the utilization of net operating loss carry-forwards of \$679,536.

The equity in losses of an affiliate in 1994 of \$144,460 was applicable to the cost of maintaining the Nevada mining properties of Pioche-Ely Valley Mines, Inc. ("Pioche-Ely Valley"). The 1994 loss was higher than usual due to an increased loss experienced by Pioche-Ely Valley on the write-off of several unpatented claims that were considered to have no future value. There was no activity in 1994 and 1993 on the Pioche-Ely Valley properties primarily due to the lack of financing for claims to be explored and developed. Interest income in 1994 and 1993 was from the investment of excess cash in Saudi Arabia and time deposits of the refinery operations. In 1994 and 1993 there was no operating activity in any of the Saudi Arabia mining properties. Assuming financing can be obtained, the results of the updated feasibility study contemplate that

construction of an ore treatment plant and all infrastructure for a mining facility will commence in 1995 and be completed in 1996. The feasibility study estimates the cost of the mining facility to be \$81.3 million.

With one exception, other income represents various items of miscellaneous income which individually are not significant enough to warrant being separately disclosed. Other income in 1994 includes \$172,737 relating to the write-off of a contingent liability established in 1992 to provide for possible future expenses relating to certain indebtedness of the coal company which were completely paid in 1994. Other items included in other income are tank rentals, building rentals, cancellation of debt income, commission income and occasional small asset sale proceeds. In 1994, the refinery collected \$101,640 from leasing an office building, a \$11,012 increase from 1993. Tank rentals increased from \$4,600 in 1993 to \$97,000 in 1994 since a new lease began in March 1994.

Primarily as a result of the Company's write-off of its total investment in the coal leases, the Company had net operating loss carry-forwards of approximately \$27.3 million at December 31, 1994, of which approximately \$14.8 million is limited to the net income of the coal company and approximately \$1.1 million of this amount is limited to the net income of TOCCO. These carry-forwards expire during the years 1994 through 2008. The Company is currently negotiating with a company toward the possible use of the coal company's amount, although there can be no assurances that any agreement relating thereto will be reached.

At December 31, 1994, a total of approximately \$1,237,000 in accrued salaries and termination benefits was due to Company employees in Saudi Arabia, which includes approximately \$586,000 due to Hatem El-Khalidi, the Company's President and Chief Executive Officer. Accrued unpaid salaries and termination benefits to Company employees in Saudi Arabia and to Mr. El-Khalidi at December 31, 1993 were approximately \$676,000 and \$507,000, respectively. These unpaid amounts have been deferred until the Company's working capital position improves.

COMPARISON OF THE YEARS 1993 TO 1992

During the fiscal year ended December 31, 1993, the Company had a net loss of \$1,338,321 compared to a net loss of \$2,195,861 for the fiscal year ended December 31, 1992.

The gross refined product sales in 1993 of \$15,103,422 was an increase of \$1,783,477 from 1992 while the cost of sales in 1993 of \$13,314,427 was an increase of \$1,463,843 from 1992, resulting in a net margin increase in 1993 of \$319,634. After processing fee income, general and administrative expenses and depreciation and amortization, the operating loss of the Company in 1993 of \$934,567 was \$92,246 less than the operating loss in 1992 of \$1,926,813. The net loss for the refining operations in 1993 of \$356,115 was \$1,410,000 less than the net loss in 1992 of \$1,661,000 (after a charge of \$975,000 for possible litigation expenses). The last five months of 1993 reflected a net profit for the refining operations.

The reduction in the size of the Refining Company's net loss in 1993 reflected the improvement in the U.S. economy, primarily over the last half of the year. Product sales volumes began to strengthen in mid-1993 due to increased activity in the industries served by the Company. The number of customers served by the Refining Company increased by 7% during 1993, and the total volume of products sold increased by 22% from 15.5 million gallons in 1992 to 18.6 million gallons in 1993. The Refining Company continued the past trend of placing the majority of its production into the higher priced premium petroleum solvent markets. During the last five years, the Refining Company has increased the percentage sold into these markets from 53% in 1989 to over 70% for each of the last three years. The ability to produce products of the quality sufficient for these higher priced markets has enabled the Refining Company to remain competitive even during down periods in the industry.

The weak economy in 1992 and early 1993 contributed to a lack of toll processing opportunities. In 1992, the Refining Company generated just over \$147,879 in toll processing revenues while 1993 toll processing revenues were \$163,977. Many in the industry have turned their focus toward complying with federal and state regulations and are not actively searching for new opportunities which would require toll processing services. This is typical of the industry during difficult times and will improve as the economy improves, although there can be no assurance to that effect.

Margins were not good for much of the year 1992 and the early part of 1993. The Clean Air Act has upset the traditional price and supply relationships of many materials in the petroleum industry. The spot price of natural gasoline, the primary feedstock for the refinery, has in the past normally fluctuated in a range of \$.08 to \$.18 per gallon below the spot price of regular unleaded gasoline. Price fluctuations in the past have depended upon the season of the year and the demand from other parts of the petrochemical industry which also might use natural gasoline for feedstock to various operations. In 1992, the demand from other segments of the petrochemical industry kept the price near the low end of the range much of the year. Demand was strong because more traditional alternative feedstocks for the industry were more scarce and higher priced due to changes brought about in the nationwide gasoline blending pool by the Clean Air Act. It is anticipated that the price relationships in the petroleum products markets will continue to find their economic levels, although there can be no assurance to that effect. During the last half of 1993, due to the oversupply of crude oil and stable demand, the prices of all petroleum products, including natural gasoline, dropped by as much as 25% from their 1992 levels. As a result, the Refining Company's margins during the last half of 1993 were greater than those experienced during the previous 18 months.

General and administrative expenses increased by \$323,176 to \$2,208,592 in 1993 from \$1,885,416 in 1992. This increase was attributable to the recording of \$478,500 for the value of stock options granted in 1993. Without this expense amount, the general and administrative expenses would have reflected a decrease of \$155,324 due to the continued cost saving measures initiated at the refinery. The expenses of regulatory compliance and reporting continue to increase. Interest expense, which is practically all attributable to the debt of the refinery, increased by \$108,017 from \$468,321 in 1992 to \$576,338 in 1993. This increase in interest expense was attributable to accrued interest of \$155,525 in 1993 on a note for which a settlement had been expected in 1992, which settlement would have provided for no

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interest. This settlement had not yet occurred. Without this adjustment, interest expense in 1993 would have decreased by \$47,508 as debt was being retired in 1993.

The equity in losses of an affiliate in 1993 of \$59,812 was applicable to the cost of maintaining the Nevada mining properties of Pioche-Ely Valley. There was no activity in 1993 and 1992 on these properties primarily due to the lack of financing for claims to be explored and developed. Interest income in 1993 and 1992 was from the investment of excess cash in Saudi Arabia and time deposits of the refinery operations. In 1993 and 1992 there was no operating activity on any of the Saudi Arabia mining properties. Assuming financing can be obtained, the preliminary results of the updated feasibility study contemplate that construction of an ore treatment plant and all infrastructure for a mining facility commence in 1994 and be completed in 1996. The preliminary results show the estimated cost of the mining facility to be \$70 million.

Other income represents various items of miscellaneous income which individually are not significant enough to warrant being separately disclosed. Such items include tank rentals, building rentals, cancellation of debt income, commission income and occasional small asset sale proceeds. In 1993 the refinery began leasing an office building and collected \$90,628. Tank rentals decreased from \$61,200 in 1992 to \$4,600 in 1993 since the lessee discontinued leasing the tanks in early 1993.

Primarily as a result of the Company's write-off of its total investment in the coal leases, the Company had a tax loss carry-forward of approximately \$27.5 million at December 31, 1993, of which approximately \$14.8 million is limited to the net income of the coal company during the years 1994 through 2008. Additionally, approximately \$3 million of this amount is limited to the net income of TOCCO. The Company will be actively seeking a method of utilizing this tax loss carry-forward.

At December 31, 1993, a total of approximately \$1,183,000 in accrued unpaid salaries and termination benefits was due to Company employees in Saudi Arabia, which includes approximately \$507,000 due to Hatem El-Khalidi, the Company's President and Chief Executive Officer. Accrued unpaid salaries and termination benefits to Company employees in Saudi Arabia and to Mr. El-Khalidi at December 31, 1992 were approximately \$625,000 and \$455,000, respectively. These unpaid

amounts have been deferred until the Company's working capital position improves.

REPORT OF INDEPENDENT ACCOUNTANTS

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

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations, of stockholders' equity and of cash flows present fairly, in all material respects, the financial position of Arabian Shield Development Company and its subsidiaries at December 31, 1994 and 1993, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 1994, 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 audits. We conducted our audits 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 audits provide a reasonable basis for the opinion expressed above.

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 4 and 6 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, 1994. None of the related projects have been developed for commercial operation as of December 31, 1994, and significant expenditures, for which the Company must obtain financing, will be necessary before commercial operations, if any, are commenced.

As described in Note 6 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 negotiate a restructuring of the loan.

As described in Notes 4 and 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 totalling \$4.5 million. South Hampton does not have the ability to 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.

As described in Note 13, in 1993 the Company changed its method of accounting for income taxes.

PRICE WATERHOUSE LLP

Dallas, Texas
 March 27, 1995

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ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

<TABLE>
 <CAPTION>

| | December 31, | |
|---|---------------|---------------|
| | 1994 | 1993 |
| <S> | <C> | <C> |
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents in United States | \$ 1,326,119 | \$ 118,828 |
| Accounts receivable (net of allowance for doubtful accounts of \$129,617 in 1994 and \$117,066 in 1993) | 1,402,982 | 1,504,116 |
| Inventories | 471,074 | 647,039 |
| | ----- | ----- |
| Total current assets | 3,200,175 | 2,269,983 |
| Cash in Saudi Arabia | 430,976 | 1,688,018 |
| Refinery plant, pipeline and equipment at cost | 5,440,208 | 5,161,086 |
| Less accumulated depreciation | (2,187,256) | (1,872,386) |
| | ----- | ----- |
| Refinery plant, pipeline and equipment, net | 3,252,952 | 3,288,700 |
| Al Masane Project and surrounding properties | 30,112,132 | 29,368,423 |
| Other interests in Saudi Arabia | 2,431,248 | 2,431,248 |
| Investment in and advances to Pioche-Ely Valley Mines, Inc. | 247,052 | 351,397 |
| Goodwill | 678,206 | 958,510 |
| Other assets (net of allowance for doubtful accounts of \$114,537 in 1994 and 1993) | 704,035 | 734,087 |
| | ----- | ----- |
| Total assets | \$ 41,056,776 | \$ 41,090,366 |
| | ===== | ===== |

</TABLE>

See notes to consolidated financial statements.

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

<TABLE>
<CAPTION>

| | December 31, | |
|---|---------------|---------------|
| | 1994 | 1993 |
| <S> | <C> | <C> |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Accounts payable | \$ 944,007 | \$ 668,300 |
| Accrued liabilities | 616,459 | 1,869,025 |
| Accrued liabilities in Saudi Arabia | 785,743 | 969,940 |
| Notes payable | 15,945,393 | 18,044,099 |
| Current portion of long-term debt | 67,968 | - |
| Current portion of long-term obligations | 18,805 | 17,278 |
| | ----- | ----- |
| Total current liabilities | 18,378,375 | 21,568,642 |
| Long-term debt | 195,386 | - |
| Long-term obligations | 206,013 | 224,445 |
| Accrued liabilities in Saudi Arabia | 585,918 | 506,997 |
| Deferred revenue | 160,693 | 176,197 |
| Commitments and contingencies | | |
| Stockholders' equity: | | |
| Common stock, authorized 40,000,000 shares of \$.10 par value; issued and outstanding, 20,028,494 shares in 1994 and 20,014,494 shares in 1993 | 2,002,849 | 2,001,449 |
| Additional paid-in capital | 32,899,119 | 32,886,519 |
| Receivables from stockholders | (276,000) | (326,000) |
| Accumulated deficit | (13,095,577) | (15,947,883) |
| | ----- | ----- |
| | 21,530,391 | 18,614,085 |
| | ----- | ----- |
| Total liabilities and stockholders' equity | \$ 41,056,776 | \$ 41,090,366 |
| | ===== | ===== |

</TABLE>

See notes to consolidated financial statements.

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF OPERATIONS
FOR THE THREE YEARS ENDED DECEMBER 31, 1994

<TABLE>
<CAPTION>

1994 1993 1992

| <S> | <C> | <C> | <C> |
|--|---------------|----------------|----------------|
| Revenues: | | | |
| Refined product sales | \$ 17,564,226 | \$ 15,103,422 | \$ 13,319,945 |
| Processing fees | 200,757 | 163,977 | 147,879 |
| Total | 17,764,983 | 15,267,399 | 13,467,824 |
| Operating costs and expenses: | | | |
| Cost of refined product sales and processing | 13,750,750 | 13,314,427 | 11,850,584 |
| General and administrative | 2,036,470 | 2,208,592 | 1,885,416 |
| Depreciation and amortization | 647,137 | 678,947 | 683,637 |
| Litigation | (975,000) | - | 975,000 |
| Total | 15,459,357 | 16,201,966 | 15,394,637 |
| Operating income (loss) | 2,305,626 | (934,567) | (1,926,813) |
| Other income (expenses): | | | |
| Interest income | 56,491 | 46,433 | 8,085 |
| Interest expense | (347,364) | (576,338) | (468,321) |
| Equity in losses of affiliate | (144,460) | (59,812) | (10,275) |
| Other income | 443,836 | 185,963 | 206,588 |
| Income (loss) before income taxes and extraordinary item | 2,314,129 | (1,338,321) | (2,190,736) |
| Income tax expense | (39,973) | - | (5,125) |
| Income (loss) before extraordinary item | 2,274,156 | (1,338,321) | (2,195,861) |
| Extraordinary item | 578,150 | - | - |
| Net income (loss) | \$ 2,852,306 | \$ (1,338,321) | \$ (2,195,861) |
| Per common share: | | | |
| Income (loss) before extraordinary item | \$.11 | \$ (.08) | \$ (.14) |
| Extraordinary item | .03 | - | - |
| Net income (loss) | \$.14 | \$ (.08) | \$ (.14) |
| Weighted average number of common shares outstanding | 20,027,881 | 17,532,335 | 15,660,893 |

</TABLE>

See notes to consolidated financial statements.

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY

<TABLE>
<CAPTION>

| | Common Stock | | Additional Paid-in Capital | Receivables From Stockholders | Accumulated Deficit | Total |
|---|--------------|--------------|----------------------------------|-------------------------------------|------------------------|---------------|
| | Shares | Amount | | | | |
| <S> | <C> | <C> | <C> | <C> | <C> | <C> |
| January 1, 1992 | 15,595,240 | \$ 1,559,524 | \$ 28,223,794 | \$ (181,000) | \$(12,413,701) | \$ 17,188,617 |
| Common stock and common stock subscriptions | 605,000 | 60,500 | 544,500 | | 605,000 | |
| Stock options issued | | 189,900 | | | 189,900 | |
| Offset of stockholder receivables with unpaid salaries | | | 55,000 | | 55,000 | |
| Other | (16,996) | (1,700) | 1,700 | | | |
| Net loss | | | (2,195,861) | (2,195,861) | | |
| December 31, 1992 | 16,183,244 | 1,618,324 | 28,959,894 | (126,000) | (14,609,562) | 15,842,656 |
| Common stock and common stock subscriptions | 3,831,250 | 383,125 | 3,448,125 | (200,000) | 3,631,250 | |
| Stock options issued | | 478,500 | | | 478,500 | |
| Net loss | | | (1,338,321) | (1,338,321) | | |
| December 31, 1993 | 20,014,494 | 2,001,449 | 32,886,519 | (326,000) | (15,947,883) | 18,614,085 |
| Common stock and common stock subscriptions | 14,000 | 1,400 | 12,600 | | 14,000 | |
| Payment on stockholder receivables | | | 50,000 | | 50,000 | |
| Net income | | | 2,852,306 | 2,852,306 | | |
| December 31, 1994 | 20,028,494 | \$ 2,002,849 | \$ 32,899,119 | \$ (276,000) | \$(13,095,577) | \$ 21,530,391 |

</TABLE>

See notes to consolidated financial statements.

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF CASH FLOWS
FOR THE THREE YEARS ENDED DECEMBER 31, 1994

<TABLE>
<CAPTION>

| | 1994 | 1993 | 1992 |
|--|--------------|----------------|----------------|
| <S> | <C> | <C> | <C> |
| Operating activities: | | | |
| Net income (loss) | \$ 2,852,306 | \$ (1,338,321) | \$ (2,195,861) |
| Adjustments for non-cash transactions: | | | |
| Depreciation and amortization | 647,137 | 678,947 | 683,637 |
| Equity in loss of affiliates | 144,460 | 59,812 | 10,275 |
| Stock options issued | - | 478,500 | 189,900 |
| Extraordinary item | (578,150) | - | - |

| | | | |
|---|--------------|-------------|-----------|
| Effects of changes in: | | | |
| Decrease (increase) in accounts receivable | 101,134 | (430,924) | 672,836 |
| Decrease (increase) in inventories | 175,965 | (124,395) | 52,117 |
| Decrease (increase) in other assets | 30,052 | 222,466 | (8,947) |
| (Decrease) increase in accounts payable and accrued liabilities | (821,334) | 46,659 | 787,701 |
| (Decrease) increase in deferred revenue | (15,504) | (15,504) | 21,658 |
| Other | 21,922 | (4,282) | 79,383 |
| | ----- | ----- | ----- |
| Net cash provided by (used for) operating activities | 2,557,988 | (427,042) | 292,699 |
| Investing activities: | | | |
| Additions to Al Masane Project and surrounding properties | (743,709) | (965,162) | (661,202) |
| Additions to other interests in Saudi Arabia | - | (41,144) | (69,333) |
| Additions to refinery plant, pipeline and equipment | (279,122) | (2,818) | (120,860) |
| (Increase) decrease in cash in Saudi Arabia | 1,257,042 | (1,674,078) | (4,457) |
| Increase (decrease) in accrued liabilities in Saudi Arabia | (105,276) | 104,947 | 372,108 |
| | ----- | ----- | ----- |
| Net cash provided by (used for) investing activities | 128,935 | (2,578,255) | (483,744) |
| | ----- | ----- | ----- |
| Financing activities: | | | |
| Common stock issued for cash | - | 3,131,250 | 105,000 |
| Decrease in receivables from stockholders | (50,000) | - | - |
| Additions to notes payable and long-term obligations | - | 70,748 | 495,076 |
| Reduction of notes payable and long-term obligations | (1,429,632) | (174,342) | (411,077) |
| | ----- | ----- | ----- |
| Net cash provided by financing activities | (1,479,632) | 3,027,656 | 188,999 |
| | ----- | ----- | ----- |
| Net increase (decrease) in cash | 1,207,291 | 22,359 | (2,046) |
| Cash and cash equivalents at beginning of year | 118,828 | 96,469 | 98,515 |
| | ----- | ----- | ----- |
| Cash and cash equivalents at end of year | \$ 1,326,119 | \$ 118,828 | \$ 96,469 |
| | ===== | ===== | ===== |

</TABLE>

See notes to consolidated financial statements.

1. BUSINESS AND OPERATIONS OF THE COMPANY

Since its organization on May 4, 1967, the principal interest of Arabian Shield Development Company (the "Company" or "ASDC") has been the exploration and development of mineral deposits in Saudi Arabia (Note 6). 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 ("ASCC") and is currently dormant. The Company, through its wholly-owned subsidiary American Shield Refining Company ("ASRC"), owns all of the outstanding common stock of Texas Oil and Chemical Company II, Inc. ("TOCCO"), and its subsidiaries, South Hampton Refining Company ("South Hampton") and Gulf States Pipeline Company, Inc. ("Gulf States"). The principal assets of TOCCO and its subsidiaries are a special products refinery located outside of Beaumont, Texas, which currently processes light naphtha feedstock, and 45 miles of natural gas and product pipelines which connect the refinery to supplies and a marine terminal on the Gulf of Mexico (Note 7). The Company also has an equity interest in Pioche-Ely Valley Mines, Inc. ("Pioche") which owns mineral deposits in Nevada (Note 8).

Prior to 1988, the Company was considered a development stage company. Although the Company has not yet commenced the principal operations for which it was formed, the significance of the refining operations led management to conclude that the Company ceased to be a development stage company effective January 1, 1988.

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 1994 were the operations of South Hampton and the proceeds from issuance of the Company's stock. The Company is not currently generating cash flow from any other activities. As described in Notes 4 and 9, the cash flow attributable to South Hampton is fully dedicated to repayment of debt and funding of refinery operations. The cash flow attributable to South Hampton currently is not adequate for these purposes. 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 (Note 16). Subsequent to the start up of operations of the Al Masane mine, anticipated in 1996, it is expected that the operations and obligations of the Company will be funded from these operations. In the event that the Company is unable to complete sales of its common stock, obtain suitable financing, and reach 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.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

PRINCIPLES OF CONSOLIDATION - All majority-owned subsidiaries are consolidated and all material intercompany accounts and transactions are eliminated. Investments in 20 to 50% owned subsidiaries and investments in subsidiaries for which greater than 50% ownership is deemed temporary are accounted for on the equity method. Investments in other companies that are less than 20% owned are accounted for on the basis of the Company's cost. In 1992, the Company began to fully consolidate the Al Masane Project (Note 6). Previously, the Company accounted for the Al Masane Project by the equity method.

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

INVENTORIES - Refined products and feedstock are carried 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, 1994, none of the projects described in Notes 6 and 8 had reached the commercial exploitation stage. No indirect overhead or general and administrative costs have been allocated to any of the projects.

REFINERY PLANT, PIPELINE AND EQUIPMENT - Beginning in 1994, all additions to refinery plant, pipeline, buildings and equipment are being depreciated on the straight-line method over useful lives of five to seven years (5 to 15 years prior to January 1, 1994). Maintenance and repairs are charged to expense. Renewals and betterments are capitalized.

OTHER ASSETS - Other assets include notes receivable from related parties, prepaid expenses, certain refinery assets which are being leased to a third party and a certificate of deposit collateralizing reclamation work on formerly owned coal leases.

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

STATEMENT OF CASH FLOWS - On the statement of cash flows, cash includes cash held in the United States. Significant noncash changes in financial position in 1994 include the issuance of 14,000 shares of common stock in exchange for the cancellation of \$14,000 of indebtedness and the forgiveness of debt and accrued interest (Note 12). Transactions of this type in 1993 include the issuance of 200,000 shares of common stock in exchange for the cancellation of \$142,099 of notes payable and \$57,901 of accrued interest, and the issuance of 300,000 shares of common stock in exchange for the cancellation of \$300,000 of indebtedness (Notes 9 and 11). Transactions of this type in 1992 include the issuance of 500,000 shares of common stock in exchange for cancellation of \$500,000 in indebtedness.

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 third quarter of 1994 which resulted in a net recognized loss of \$117,000 during 1994. This loss is included as a cost of refined product sales and processing in the consolidated statement of operations. As of December 31, 1994, South Hampton has incurred \$65,000 of unrecognized losses related to its open contracts. These contracts expire within the next twelve months.

PER SHARE DATA - Net income (loss) per share has been computed on the basis of the weighted average number of shares of common stock outstanding during the year.

FOREIGN CURRENCY - Assets and liabilities denominated in foreign currencies, principally Saudi Riyals, are translated at rates in effect at the time the transaction occurred. There has been no change in the exchange rate for Saudi Riyals to the United States dollar during the period covered by these financial statements.

INCOME TAXES - In the first quarter of 1993, the Company adopted Statement of Financial Accounting Standards No. 109, "Accounting for Income Taxes" ("SFAS No. 109"). SFAS No. 109 requires the Company to

compute deferred income taxes based on the amount of taxes payable in future years, after considering changes in tax rates and other statutory provisions that will be in effect in those years. The provision for income taxes includes taxes currently payable and those deferred because of temporary differences between the financial statement and tax bases of assets and liabilities. The adoption had no significant impact on 1993 earnings or cash flow.

Deferred income taxes in 1992 were provided in accordance with Accounting Principles Board Opinion No. 11 ("APB Opinion No. 11"). Timing differences resulted principally from depreciation of property and equipment.

GOODWILL - Goodwill acquired in connection with the acquisition of TOCCO is being amortized over ten years. The amounts reflected in the balance sheet are net of accumulated amortization of \$2,104,809 and \$1,824,505 at December 31, 1994 and 1993, respectively. The Company periodically reviews goodwill for any permanent impairment in value or life.

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.

RECLASSIFICATIONS - Certain prior year amounts have been restated to conform to the current year presentation.

4. 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 6 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.

On November 14, 1990, Cajun Energy, Inc. ("Cajun Energy"), a distributor of refined gasoline to retail stations, filed a lawsuit alleging South Hampton manufactured and sold defective gasoline and/or failed to properly test its product prior to sale to Cajun Energy. Prior to initiation of this lawsuit by Cajun, claims in excess of \$906,000 were paid by South Hampton's insurance carrier under a \$1 million liability policy.

E-Z Mart Stores filed a lawsuit on May 22, 1991 against Cajun Energy and South Hampton related to the aforementioned manufacture and sale of alleged defective gasoline. E-Z Mart Stores claimed that defective gasoline was distributed to its stores in late April and May 1990 resulting in customers suffering damage to their automobiles.

South Hampton filed suit on August 18, 1992 in the 58th Judicial District Court, in Jefferson County, Texas against National Union Fire Insurance Company, ("National Union") as the insurance carrier for a second named party in the Cajun Energy litigation, for failing and refusing to defend South Hampton in the two causes of action described above. South Hampton had asserted that it was an additional named insured on the insurance policy provided to this second named party in the litigation described above and that the insurer should have provided defense to the claims asserted.

In May 1994, the E-Z Mart Stores lawsuit went to trial and a judgement was entered against South Hampton. In consideration of the judgement and, since the issues were identical to the claims asserted in the Cajun Energy lawsuit, there has been a dismissal by Cajun Energy of its lawsuit against South Hampton. At the trial, South Hampton consented to a settlement agreement whereby E-Z Mart Stores and Cajun were awarded a judgement against South Hampton for approximately \$6 million. E-Z Mart Stores and Cajun signed a "nonexecution agreement" not to execute the judgement in return for the assignment by South Hampton of its claims against National Union. South Hampton has also agreed not to pursue its 1992 lawsuit against National Union. This concluded the claims and actions against South Hampton in these matters.

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

South Hampton is involved as a defendant in other litigation incident to its activities. The outcome of these matters is not expected to have a material impact on the Company's financial position or results of operations.

South Hampton has short-term notes payable and current portions of long-term obligations totalling \$4.5 million, of which \$2.9 million relate to bank financing which has historically been renewed in six-month intervals and is not guaranteed by the Company. South Hampton does not currently have the ability to repay these current obligations from the level of internally generated funds. Any cash flow generated by the refinery is fully dedicated to the repayment of debt and funding of refining operations. In order to satisfy these obligations in an orderly manner, management of South Hampton must: (1) obtain a renewal of the bank debt (see Note 9) and have continued forbearance by the bank with respect to debt covenants and provisions, and (2) generate increased cash flows from refinery operations to service debt obligations and fund other working capital needs of the refinery.

Should South Hampton not meet its cash flow requirements during 1995, management believes that it will be able to obtain modifications of the repayment terms of the debt obligations. Management believes that additional funds may be obtained from the proceeds of future common stock sales or the sale of all or a partial interest in South Hampton. On March 16, 1992, the Company received an offer from a Saudi Arabian company, also a related party, to purchase all of the issued and outstanding shares of TOCCO for \$2,230,000, which was rejected due to its unfavorable terms. The Company's financial statements do not include any adjustments that might be necessary should South Hampton be unable to satisfy its obligations in an orderly manner.

ASCC has been a responsible party for certain reclamation work on coal properties which it previously leased. ASCC had provided a letter of credit secured by a \$36,000 certificate of deposit to the Mined Land Reclamation Division of Colorado in connection with this liability. In March 1994, the Mined Land Reclamation Division exercised its rights under the letter of credit and ASCC paid the \$36,000. This concluded ASCC's involvement in the reclamation project.

South Hampton has been spending an increased amount of time and expense

on environmental and regulatory functions and compliance. In mid-1993, while remediating a small spill area, the Texas Natural Resources Conservation Commission ("TNRCC") requested the refinery to drill a well to check the groundwater under the refinery property to ensure that contamination had not taken place. The well disclosed a pool of hydrocarbons on top of the groundwater under the loading rack area. An analysis of the material indicated that the hydrocarbons were produced over ten years ago when the refinery processed crude oil. Consulting engineers were hired to determine the size of the pool. Three recovery wells were utilized and the hydrocarbons are being pumped out and treated in treatment ponds. The TNRCC has been cooperating in the investigation and cleanup. Due to the apparent age of the material, no fine or enforcement action is expected. A site assessment plan is being developed to determine the extent of the hydrocarbon pool. The costs through 1994 for this problem totaled approximately \$35,000. Future costs for recovery and remediation should be small as it is primarily a matter of operating the recovery wells.

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

In August 1994, the TNRCC's Air Permit Section proposed a fine of approximately \$46,000 to settle various alleged permit violations identified in their 1991, 1992 and 1993 inspections. South Hampton agreed to the proposed settlement with the stipulation that payments be spread over a twelve month period. The Commission has not yet formally adopted the agreement. In October 1994, the TNRCC formally adopted an agreement with South Hampton to settle alleged water violations regarding monitoring water wells with a fine of \$9,600 to be paid over four months and a deferred fine of \$9,600 to be dependent upon the future operation of a bioremediation site.

In addition to the various Environmental Protection Agency and TNRCC air, water and solid waste regulations, South Hampton is also subject to the regulations of the U.S. Department of Transportation, 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 meeting the requirements of the OSHA Process Safety Management rules. By the time these various agency requirements are met, it is expected that South Hampton will spend in excess of \$100,000 over the eighteen month period ending May 1995 to develop the procedures and documentation required.

5. INVENTORIES

Inventories include the following:

<TABLE>

<CAPTION>

| | December 31, | |
|--------------------|--------------|------------|
| | 1994 | 1993 |
| | ----- | ----- |
| | 1994 | 1993 |
| | ----- | ----- |
| <S> | <C> | <C> |
| Refinery feedstock | \$ 226,265 | \$ 298,928 |
| Refined products | 244,809 | 348,111 |
| | ----- | ----- |
| Total inventories | \$ 471,074 | \$ 647,039 |
| | ===== | ===== |

</TABLE>

In 1994, a liquidation of LIFO inventory quantities carried at lower costs prevailing in prior years decreased cost of goods sold and increased net income by approximately \$57,000. At December 31, 1994,

market value exceeded LIFO value by approximately \$193,000. At December 31, 1993, LIFO value approximated market value.

6. 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. "Al Masane Project and surrounding properties" primarily pertains to the Al Masane Project (the "Project"), but also includes costs attributable to the interests in the Greater Al Masane areas. "Other interests in Saudi Arabia" primarily pertains to the costs of rentals, field offices and camps, core drilling and labor incurred at the Wadi Qatan and Jebel Harr properties.

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

In 1971, the Saudi Arabian government awarded exploration licenses to the Company and National Mining Company ("NMC"), a Saudi Arabian company, for the Al Masane Project, Wadi Qatan and Jebel Harr areas. Until April 1992, the Company and NMC each held a 50% interest in the exploration licenses. The Company and NMC also obtained written authority to explore an area of 1,100 square kilometers surrounding Al Masane ("Greater Al Masane"). The Saudi Arabian government has verbally indicated that an exploration license for Greater Al Masane will be granted (unaudited).

Prior to 1979, the Company funded all costs related to these properties. In 1979, the Company formed a joint venture with NMC related to the Al Masane Project in which each company held a 50% interest in the exploration license. The joint venture obtained an \$11 million interest-free loan from the Saudi Arabian government which was scheduled to be repaid in ten equal annual installments beginning December 1984. None of the scheduled payments have been made. The proceeds from this loan were used to fund the costs of the Project. Other than the use of the proceeds from the loan, subsequent to the formation of the joint venture with NMC, 100% of the exploration costs of the Project as well as all exploration costs for the other interests continued to be funded by the Company.

In 1992, NMC relinquished its rights to the exploration license and the mining lease in the Al Masane area, and assigned them to the Company. The Company accepted the conditions set by the Saudi Arabian government in a letter dated March 30, 1992. In connection with NMC's assignment of its interest to the Company, the Company agreed to provide for public subscription in Saudi Arabia of 50% of the capital of the Project at such time as the Project proves to be commercial. On April 13, 1992, the Company and NMC signed an agreement dissolving the joint venture and NMC assigned its rights and obligations to the exploration license and the mining lease in the Al Masane area to the Company. Subsequently, a formal Mining Lease Agreement assigning the lease solely to the Company was initialled by the Company and the Ministry on October 4, 1992.

Prior to April 13, 1992, the Company had accounted for its interest in the Al Masane Project on an equity basis and its investment in the joint venture was recorded at the amount of the owners' capital of the joint venture. When the joint venture was dissolved, the Company consolidated the Al Masane Project by eliminating the related investment balance against the owners' capital account of the Project, and by recording the assets and liabilities of the Project (including the \$11 million loan) in the consolidated balance sheet.

Since NMC assigned its 50% interest in the exploration license and any resulting mining lease to the Company, the Company is solely responsible for the repayment of the \$11 million loan. Pursuant to Article 15 of the Mining Lease Agreement which was initialled on October 4, 1992, the loan is to be rescheduled to be repaid from the profits of the mining operations after the mining lease is issued to the Company. A

rescheduling of the loan payments has not yet been negotiated. All of the Company's assets in Saudi Arabia are pledged as collateral for the loan.

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

If exploration licenses for Wadi Qatan, Jebel Harr or Greater Al Masane (which includes Jabal Guyan) are converted to mining leases, NMC will reimburse the Company for its share of costs (as defined in an agreement between the parties). The Company has had positive results from its exploration work at these sites; however, it has directed limited amounts of time and resources on these sites in recent years while it has negotiated with the Saudi government for the Al Masane lease. The Company intends to negotiate agreements for these sites in the near future, does not intend to abandon these sites, and considers the costs deferred at December 31, 1994 to be recoverable.

The Company had filed in 1984 with the Council of Ministers of the Saudi Arabian government for a mining lease for the Al Masane Project based on the presumption that commercial productibility had been proven. On April 26, 1993, the Council of Ministers passed the resolution granting the Company the mining lease, and on May 22, 1993, a Royal Decree was issued by the King. The initial period of 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. An amendment was made in the lease agreement which stipulates that, when the profitability of the project is demonstrated, a Saudi public stock company will be formed and the Company will contribute its investment in the Al Masane Project in return for 50% of the stock of the Saudi 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 in the Saudi company and the remaining interests not owned by the Company or acquired by PETROMIN are to be put out for public subscription to Saudi citizens.

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 McOuat Limited, consulting geologist, indicating the commercial viability of the Project. The 1994 report estimates proven and probable reserves of copper, zinc, silver and gold of 7.2 million tons in the Al Masane area with the potential to increase these reserves with further exploration. The report projects production of the proven and probable reserves over a twelve-year period commencing in 1996. The 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 in connection with the public subscription in Saudi Arabia. Revenues were estimated utilizing projected mineral prices from a third party pricing expert. The report projects positive net cash flows to the Company of \$37 million over the life of the Project. It is not anticipated that taxes will be paid to the Saudi government in the first five years of production of the Project. (unaudited)

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Deferred development costs of the Al Masane Project and surrounding areas at December 31, 1994, 1993 and 1992, and the changes in these amounts for each of the three years then ended are detailed below:

<TABLE>
<CAPTION>

| | Balance at December 31, 1994 | Activity for 1994 | Balance at December 31, 1993 | Activity for 1993 | Balance at December 31, 1992 | Activity for 1992 |
|--|------------------------------------|-------------------------|------------------------------------|-------------------------|------------------------------------|-------------------------|
| <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 and project administration costs | 16,023,275 | \$ 237,908 | 15,785,367 | \$ 653,930 | 15,131,437 | \$ 564,407 |
| Materials and maintenance | 6,161,684 | 683 | 6,161,001 | 1,232 | 6,159,769 | 71,801 |
| Feasibility study | 2,626,474 | 505,118 | 2,121,356 | 310,000 | 1,811,356 | 24,994 |
| Total | 24,811,433 | 743,709 | 24,067,724 | 965,162 | 23,102,562 | 661,202 |
| | \$ 30,112,132 | \$ 743,709 | \$ 29,368,423 | \$ 965,162 | \$ 28,403,261 | \$ 661,202 |

</TABLE>

The Company has not made all of the surface rental payments due to the government of Saudi Arabia under the terms of the Al Masane Project lease. At December 31, 1994, the past due amount of these rent payments is approximately \$74,000. 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 license requirements will not have any effect on the Company's planned operations in Saudi Arabia.

Since cash in Saudi Arabia is generally intended for the support and development of the Saudi Arabian projects, a long-term asset, such cash and certain associated liabilities relating to the Saudi Arabian projects have been classified as noncurrent.

7. REFINERY OPERATIONS

South Hampton, the Company's only revenue producing asset, sells its products primarily to companies in the petroleum industry. Downturns in the petroleum industry could negatively impact refinery operations in the future. South Hampton does not require collateral on its outstanding accounts receivable balances. South Hampton's largest customer accounted for 13%, 16% and 11% of total sales in 1994, 1993 and 1992, respectively.

8. INVESTMENT IN PIOCHE-ELY VALLEY MINES, INC.

The Company effectively controls approximately 55% and directly owns approximately 46% of the outstanding common stock of Pioche. During 1988, approximately 634,000 shares of Pioche stock were deemed acquired through in-substance foreclosure on a \$114,000 note due from the issuer's estate. The note balance was reclassified to Other Assets and was fully reserved in 1989. This note is due in 1995; however, management of the

Company intends to postpone the due date indefinitely if the issuer's estate is unable to repay the note in 1995. At this point, it is not possible to determine whether the issuer's estate will repay the note and claim these shares. If it is determined that the note will not be repaid, the Company will consolidate Pioche as a majority-owned subsidiary. The principal assets of Pioche are an undivided interest in 48 patented and 84 unpatented mining claims and a 300 ton-per-day mill located on the aforementioned properties in the Pioche Mining District in southeastern Nevada. 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 in 1995.

In 1991 and 1992, the Company leased its Wide Awake Mine property to a joint venture under an agreement which called for annual rental payments of \$5,000 and a 7% royalty on net smelter returns. The annual advance rental was received for 1992 and 1991 but the joint venture did not commence any operations on the property. In December 1992, the agreement was terminated. In August 1993, Pioche entered into a new lease of the Wide Awake mine property with the same joint venture to which it had previously leased the property. This agreement stipulates a 6% royalty on net smelter returns with no annual rental required. The lease commenced on October 1, 1993, for a primary term of twenty-seven months, and will continue as long as minerals are produced in commercial quantities or unless terminated by the parties. No royalties were earned in 1994.

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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>

| | 1994 | 1993 |
|---|---------------|---------------|
| | ----- | ----- |
| <S> | <C> | <C> |
| Notes payable: | | |
| Revolving bank note. See (A) | \$ 2,927,113 | \$ 3,934,036 |
| Secured note to Saudi Arabian government. See (B) | 11,000,000 | 11,000,000 |
| Unsecured note to a Saudi company. See (C) | 1,500,000 | 1,500,000 |
| Unsecured note to a Saudi investor. See (D) | 168,280 | 168,280 |
| Unsecured note to a Saudi investor. See (E) | 350,000 | 350,000 |
| Unsecured installment note. See (F) | - | 597,625 |
| Bank note payable. See (G) | - | 360,702 |
| Other | - | 133,456 |
| | ----- | ----- |
| Total | \$ 15,945,393 | \$ 18,044,099 |
| | ===== | ===== |
| Long-term debt: | | |
| Bank note. See (H) | \$ 263,354 | |
| Less current portion | 67,968 | |
| | ----- | |
| Long-term debt | \$ 195,386 | |
| | ===== | |

Long-term obligations:
Noninterest-bearing note to a supplier and

| | | | | |
|--|----|---------|----|---------|
| customer for capital improvements. See (I) | \$ | 128,683 | \$ | 128,683 |
| Other financing obligations: | | | | |
| Deferred compensation contracts. See (J) | | 96,135 | | 113,040 |
| | | ----- | | ----- |
| Total long-term obligations | | 224,818 | | 241,723 |
| Less current portion | | 18,805 | | 17,278 |
| | | ----- | | ----- |
| Long-term obligations | \$ | 206,013 | \$ | 224,445 |
| | | ===== | | ===== |

</TABLE>

(A) In 1990, South Hampton and a bank entered into an Amended and Restated Credit Agreement ("the Agreement") in order to modify certain provisions and embody all amendments of the previous agreement in one document. 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 used to refinance the previous note, 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.)

The note is collateralized by all of the assets of TOCCO and its subsidiaries and a pledge of TOCCO stock by ASRC. In addition, the Company and ASRC have subordinated intercompany accounts receivable of approximately \$1,363,355 at December 31, 1994 to

the bank debt, and no other funds are to be advanced to the Company or ASRC by TOCCO or its subsidiaries. In the event of an enforcement by the bank of the security interests on the collateral under the Agreement, the proceeds from the security interests in the cash, accounts receivable and inventory of South Hampton will first be used to repay 60% of the outstanding principal and interest under the Agreement with any remaining proceeds used to repay any amounts owed by South Hampton to the related party due to the draw down by the bank of the letters of credit for Facility B. Any amounts recovered through other forms of collateral are to be used first to repay any remaining amounts due to the bank for principal and interest, and remaining amounts, if any, are to be used to repay any amounts still owed to the related party. South Hampton was not in compliance with the borrowing base ratio and was in default in its loan repayments at various times in 1993 and 1992.

Facility A was to be repaid under the initial agreement by June 30, 1992. South Hampton did not have adequate resources to pay the full amount outstanding during 1992. The maturity date has been extended at various times subsequent to default and has currently been extended to June 30, 1995. In connection with the latest extension, South Hampton has agreed to make quarterly principal payments of \$200,000, and Arabian Shield Development Company has committed to use its best efforts to obtain new equity financing of at least \$1,500,000 by June 30, 1995, to be remitted to the bank. Additionally, South Hampton has agreed to collect all receivables through a cash collateral account at a local bank. Only the amount of funds required to operate South Hampton's business may be used and weekly reports of cash receipts and disbursements in the cash collateral account must be provided to the creditor. If South

Hampton defaults on the credit agreement, the creditor has the right to freeze the funds in the cash collateral account. The note is subject to interest at the London Interbank Eurocurrency Market (LIBOR) rate 6.0% and 3.21875% at December 31, 1994 and 1993, respectively, plus 2%.

- (B) On January 24, 1979, the Company and NMC jointly obtained an interest-free loan of \$11,000,000 from the Saudi Arabia Ministry of Finance and National Economy 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. On April 13, 1992, NMC agreed to assign all its rights and obligations in the Al Masane Project (including its 50% obligation for the \$11,000,000 loan) to the Company. The Company is now solely responsible for the repayment of the loan. Pursuant to the mining lease agreement, the loan will be rescheduled to be repaid from the profits of the mining operations when they commence. An agreement has not yet been reached regarding the rescheduling of these payments. The loan is secured by all of the Company's 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 \$1,500,000 is now owed by South Hampton to Saudi Fal. This note is collateralized as discussed in (A) above.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

- (D) Represent noninterest demand loans payable to a Saudi investor.
- (E) Represents an advance made by a Saudi investor in 1984 to the Al Masane Project on behalf of NMC. Prior to 1992, since NMC had no liability for exploration costs unless the exploration license was converted to a mining lease, the advance was classified as a deferred capital contribution on the separate Al Masane balance sheet. Due to the relinquishment of NMC's rights and obligations in the license and the mining lease in March of 1992, the advance is now classified as an unsecured noninterest demand debt.
- (F) In 1991, South Hampton issued a note payable to a vendor to establish payment terms for past-due trade accounts payable. The note was payable in monthly installments with all amounts owed due by February 25, 1993. In May 1994 the principal balance and \$156,000 accrued interest payable under the terms of this note was settled by a \$175,000 cash payment. Accordingly, the Company recorded an extraordinary gain of \$578,150 in 1994, for which there is no tax effect after application of operating loss carryforwards, which represents the amount of trade payables forgiven.
- (G) All unpaid principal and interest related to this bank loan was due and payable in December 1994. TOCCO was in arrears with its payments in the prior and current year. Effective December 31, 1994, all unpaid principal and interest was refinanced by another bank and the Company's obligation under this note was satisfied. See (H) below.
- (H) This note payable is 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 has been leased to a third party. The original balance of the note was due and payable on December 31, 1994. This note was refinanced effective December 31, 1994 with principal and interest payments starting in March 1995 and each month thereafter until February 1, 1998. The note bears interest of 10% from the date of the agreement to February 1, 1996 and at prime rate + 1 1/2% thereafter.

- (I) Balance represents amount due under a note payable to an unrelated refining company that provided loans to the refinery to fund certain refining processes. Repayment is to be made when certain feed rate criteria and number of days of operations have been reached.
- (J) In connection with the acquisition of TOCCO, deferred compensation contracts between TOCCO and certain former employees and one current employee were restructured, reducing the gross payments due under the existing 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. Currently, all contracts have been fully satisfied except for the contracts of one current and one former employee. TOCCO has complied with the terms of these contracts through 1994. If TOCCO were to default on these contracts, it would be liable for an additional amount of \$458,000. The recorded liability has been determined utilizing a discount rate of 8.0%.

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Scheduled maturities of long-term debt and long-term obligations, which exclude current notes payable balances aggregating \$15,945,393, for the next five years and thereafter are as follows:

| | |
|------------|------------|
| <TABLE> | |
| <S> | <C> |
| 1995 | \$ 86,773 |
| 1996 | 234,008 |
| 1997 | 115,912 |
| 1998 | 30,274 |
| 1999 | 0 |
| Thereafter | 21,205 |
| | ----- |
| Total | \$ 488,172 |
| | ===== |

</TABLE>

Interest of \$275,561, \$472,131 and \$343,058 was paid in 1994, 1993 and 1992, respectively.

10. COMMITMENTS

South Hampton entered into an arrangement in July 1991 with a partnership, in which Silsbee Trading and Transportation Corp. ("STTC", a company owned by the president and vice president of TOCCO) and M.A. Bomer (the former owner of the refinery) each owned a 50% interest, to facilitate the future purchase of feedstock. Feedstock was purchased by South Hampton from the partnership at a price equal to the cost of the feedstock to the partnership plus two cents per gallon. Approximately 4,977,000 gallons of feedstock were purchased in 1992 under the terms of this agreement at a cost of approximately \$2,320,000. In June 1992, Mr. Bomer withdrew from the partnership and it was terminated. On July 1, 1992, South Hampton entered into a new agreement with STTC whereby STTC financed the feedstock in the pipeline. As a result, South Hampton has a

liability to STTC for the cost of the 453,600 gallons of capacity of the pipeline. This amount is \$215,460 and \$217,048 at December 31, 1994 and 1993, respectively. Also in connection with this agreement, South Hampton pays a one-half cent per gallon fee to STTC on each gallon of feedstock transported through the pipeline. The agreement is currently operating on a month to month basis. The fees paid by South Hampton to STTC pursuant to this agreement were \$103,212, \$88,974 and \$21,525 in 1994, 1993 and 1992, respectively.

South Hampton leases vehicles and equipment for use in operations for \$24,140 per month plus certain reimbursed costs from STTC under a lease agreement. The lease agreement expired in September 1994 and is currently continuing on a month-to-month basis. South Hampton incurred costs (most of which are billed to customers) related to this agreement of approximately \$341,000, \$320,000 and \$291,000 in 1994, 1993 and 1992, respectively. Accounts payable to STTC under the leasing arrangement were \$16,917 and \$2,431 at December 31, 1994 and 1993, respectively.

The Company incurred rental expenses for office space, one automobile and other vehicles and equipment of approximately \$302,000 in 1994 and 1993, and \$305,000 in 1992.

In February 1993, South Hampton entered into an agreement to lease to a third party a building with a net book value at December 31, 1994 of \$324,591 which South Hampton does not use in its operations. The lease provides for an option to the lessee to purchase the building after three or five years. The lease is being recorded as an operating lease and the building is

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

included in other assets. As described in Note 9, the leased building is pledged as collateral for a note payable. Other income for 1994 and 1993 includes \$102,000 and \$87,000, respectively, of rental income pursuant to this lease.

A provision of the purchase agreement related to the acquisition of TOCCO by ASRC 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.

11. COMMON STOCK AND STOCK OPTIONS

At December 31, 1994, Saudi Arabian investors owned approximately 62% 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. Proceeds from certain common stock sales were used to finance the acquisitions of ASRC and to finance the expansion of the refinery. 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. Estimates of fair values of the Company's unregistered common stock are made by management.

Notes receivable from stockholders for the purchase of common stock of \$276,000 in 1994 represent a note from a director and officer for \$126,000 which matures on December 31, 1995 and a note from an entity controlled by a stockholder for \$200,000 with a balance of \$150,000 at December 31, 1994. The note for \$200,000 was issued in March 1993 and was due in October 1994. Payments of \$50,000 were received on this note

in 1994 and management of the Company expects to collect the remaining balance in 1995. Notes receivable from stockholders are classified as a debit in 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 nonincentive 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.

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 Non-Employee Director Plan was instituted in 1987 and has

a duration of ten years. Options granted under this plan become exercisable in 20% increments each year and are granted for a ten year period. The number of shares reserved for issuance under this plan is 100,000.

On March 20, 1992, the Compensation Committee of the board of directors approved an option replacement program which permitted holders of outstanding options under the Employee Plan to surrender and cancel the options held by them and to receive in exchange new options covering an equal number of shares having an exercise price equal to the market price of the Company's common stock on March 20, 1992. Under the option replacement program, two officers and directors surrendered for cancellation the outstanding options held by them and in exchange received new options covering 70,000 shares having an option exercise price of \$1.38 per share, the market price on the date of grant. On the same date, another officer was granted an option covering 10,000 shares in exchange for the surrender and cancellation of an existing option covering 5,000 shares. On the same date, an officer of TOCCO surrendered for cancellation an outstanding option and in exchange received a new option covering 10,000 shares. On the same date, another officer of TOCCO was granted a new option covering 10,000 shares. These options also have an exercise price of \$1.38 per share, the market price on the date of the grants.

In 1993, four new directors were elected to the Company's board of directors. Pursuant to the Company's Non-Employee Director Plan, each director received on election an option for 10,000 shares of common stock at an exercise price equal to the fair market value of the stock at the date of grant. In December 1993, one of the new directors did not stand for reelection at the Company's annual stockholders' meeting and, by the terms of the Non-Employee Director Plan, his option expired in July 1994. In January 1994, another of the new directors resigned from the board and his option expired in August 1994.

On September 26, 1994, the Compensation Committee of the board of directors approved the granting of options to purchase a total of 75,000 shares of common stock for \$1.75 per share, the market value on the date of the grant, to four employees of the Company. These options expire in 2004.

A summary of stock option transactions under the Employee Plan and

Non-Employee Director Plan is as follows:

| <S> | <C> |
|--------------------------------------|----------|
| Outstanding December 31, 1991 | 105,000 |
| Granted (\$1.38 per share) | 100,000 |
| Expired | (85,000) |
| | ----- |
| Outstanding December 31, 1992 | 120,000 |
| Granted (\$2.88 to \$3.75 per share) | 40,000 |
| | ----- |
| Outstanding December 31, 1993 | 160,000 |
| Granted (\$1.75 per share) | 75,000 |
| Expired | (20,000) |
| | ----- |
| Outstanding at December 31, 1994 | 215,000 |
| | ===== |

</TABLE>

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

At December 31, 1994, 161,500 options were exercisable at prices ranging from \$1.38 to \$3.75 per share. Under these plans, 385,000 shares are available for grant. 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.

The Company granted a creditor (a company owned by the wife and other relatives of the Company's president) two, three-year options, which expired December 31, 1991, to purchase an aggregate of 1,000,000 shares at \$1.00 per share. In January 1992, these options were extended to March 1992. They were not exercised and the options expired. In March 1992, the Company granted the creditor an option to purchase 200,000 shares of common stock at \$1.00 per share to expire in December 1995. In July 1993, the creditor exercised the option and the shares were issued in exchange for the cancellation of \$200,000 of an outstanding debt.

On May 1, 1992, in consideration for a personal loan of \$200,000 from a Saudi investor who is the president of two Saudi Arabian government charitable organizations, the Board granted to the organizations an option to purchase 1,500,000 shares at \$1.00 per share by August 8, 1992 provided that these organizations accepted a previous Company offer for them to purchase 1,500,000 shares at \$1.00 per share by May 8, 1992. On September 17, 1992, in consideration for an additional loan of \$50,000 from the investor, the Board of Directors extended both the offer to sell the shares and the exercise period of the option to December 15, 1992. In consideration for an additional loan from the investor of \$50,000 in January 1993, the board of directors extended both the sell offer and the option offer to March 29, 1993. On March 23, 1993, the offers were further extended without an expiration date. On May 13, 1993, the organizations elected not to exercise these options and the options were cancelled. Concurrent with this decision, the board of directors approved a sale of 3,000,000 shares at \$1 per share to the Saudi investor. The shares were purchased by the payment of \$2.7 million in cash and the cancellation of the \$300,000 of indebtedness to the investor by the Company.

On January 21, 1992, a director and officer of the Company was granted a two-year option to purchase 14,000 shares at \$1.00 per share. In January 1994, the option was exercised and the shares were issued in exchange for

the cancellation of \$14,000 of unpaid compensation. In May 1992, a Saudi investor purchased 35,000 shares of stock at \$1.00 per share and was granted an option until December 31, 1992 to purchase an additional 35,000 shares at \$1.00 per share. The option was not exercised and has expired. On December 29, 1992, the Board approved an extension of an option to a U.S. investor to buy 46,250 shares at \$1.00 per share from December 31, 1992 to June 30, 1993. In June 1993, the option was exercised.

In March 1993, the board of directors approved the sale of 75,000 shares of common stock at \$1.00 per share to a company controlled by a director of the Company, and the grant of an option to such company to purchase 300,000 shares of common stock at \$1.00 per share, which was exercisable on or before September 10, 1993. The option for the 300,000 shares was exercised in September 1993. For the issuance of the 300,000 shares, the Company received \$100,000 in cash and a receivable from this related party of \$200,000 which has been recorded as a debit in the stockholders' equity section of the consolidated balance sheet. This receivable balance is \$150,000 at December 31, 1994.

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

A summary of stock option transactions with individuals is as follows:

| <TABLE> <S> | <C> |
|----------------------------------|-------------|
| Outstanding December 31, 1991 | 1,746,250 |
| Granted (\$1.00 per share) | 1,899,000 |
| Expired | (1,735,000) |
| | ----- |
| Outstanding December 31, 1992 | 1,910,250 |
| Granted (\$1.00 per share) | 300,000 |
| Exercised (\$1.00 per share) | (546,250) |
| Expired or forfeited | (1,650,000) |
| | ----- |
| Outstanding December 31, 1993 | 14,000 |
| Exercised | (14,000) |
| | ----- |
| Outstanding at December 31, 1994 | -0- |
| | ===== |

</TABLE>

All stock sold to individuals in connection with these options includes a restriction that it cannot be traded for a three year period.

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 and market prices. 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.

12. EXTRAORDINARY ITEM

In May 1994, South Hampton settled its note payable and accrued interest payable to a vendor for \$175,000 cash. An extraordinary gain of \$578,150, for which there is no tax effect after application of operating loss carryforwards, was recorded, representing the amount of trade accounts payable and accrued interest forgiven. See Note 9 (F).

13. INCOME TAXES

INCOME TAXES - In January 1993, the Company adopted SFAS No. 109. The adoption had no significant impact on earnings or cash flow.

The income (loss) before income taxes and extraordinary item was \$2,314,129, (\$1,338,321) and (\$2,190,736) for the years ended December 31, 1994, 1993 and 1992, respectively.

The Company's provision for income taxes was comprised of the following:

<TABLE>
<CAPTION>

| | 1994 | 1993 | 1992 |
|--|------------|--------|----------|
| <S> | <C> | <C> | <C> |
| Federal | | | |
| Current | \$ 522,938 | \$ - | \$ 5,125 |
| Deferred | - | - | - |
| Utilization of operating loss carryforward | (482,965) | - | - |
| | ----- | ----- | ----- |
| Provision for income taxes | \$ 39,973 | \$ -0- | \$ 5,125 |
| | ===== | ===== | ===== |

</TABLE>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

In years prior to 1993, the Company accounted for income taxes in accordance with APB Opinion No. 11. In 1992, the Company had significant net operating loss carryforwards to fully offset the effects of the timing differences (attributable principally to depreciation of property and equipment) which existed between financial and regular income tax reporting. However, the Company was required to provide alternative minimum tax.

Income tax expense (benefit) for the years ended December 31, 1994 and 1993 differs from the amount computed by applying the applicable U.S. corporate income tax rate of 34% to net income (loss) before income taxes (excluding the cumulative effect of the change in accounting for income taxes). The reasons for this difference are as follows:

<TABLE>
<CAPTION>

| | 1994 | 1993 |
|-------------------------------------|------------|--------------|
| <S> | <C> | <C> |
| Income taxes at U.S. statutory rate | \$ 786,804 | \$ (455,029) |
| Goodwill | 95,303 | 95,303 |
| Liability reserves | (392,700) | - |
| Net operating losses | (482,965) | 359,726 |
| Alternative minimum tax | 39,973 | - |
| Other items | (6,442) | - |
| | ----- | ----- |
| Total tax expense | \$ 39,973 | \$ -0- |
| | ===== | ===== |

</TABLE>

In 1992, income taxes differed from the statutory tax rate due to goodwill amortization, equity investment loss and unutilized tax loss carryforwards.

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities for 1994

and 1993 were as follows:

<TABLE>
<CAPTION>

| | December 31, 1994 | December 31, 1993 | January 1, 1993 |
|--|----------------------|----------------------|--------------------|
| <S> | <C> | <C> | <C> |
| Deferred tax liabilities: | | | |
| Refinery plant, pipeline and equipment | \$ (379,668) | \$ (434,700) | \$ (407,754) |
| Gross deferred tax liability | (379,668) | (434,700) | (407,754) |
| Deferred tax assets: | | | |
| Accounts receivable | 44,070 | 40,973 | 33,888 |
| Mineral interests | 196,446 | 202,224 | 202,224 |
| Net operating loss carryforwards | 9,277,552 | 9,791,240 | 9,400,963 |
| Tax credit carryforwards | 650,907 | 1,640,037 | 1,640,037 |
| Gross deferred tax assets | 10,168,975 | 11,674,474 | 11,277,112 |
| Valuation allowance | (9,789,307) | (11,239,774) | (10,869,358) |
| Net deferred tax assets | 379,668 | 434,700 | 407,754 |
| Net deferred taxes | \$ -0- | \$ -0- | \$ -0- |

</TABLE>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

As a result of current year operations, the Company's net deferred tax asset decreased by \$55,032 to \$379,668 at December 31, 1994. However, there was no change in judgment about the Company's ability to realize its net deferred tax asset; therefore, the valuation allowance was decreased by a corresponding amount.

At December 31, 1994, the Company had approximately \$27,287,000 of net operating loss carryforwards and approximately \$610,000 of general business credit carryforwards. These carryforwards expire in 1995 through 2008. In addition, the Company has minimum tax credit carryforwards of approximately \$40,000 that may be carried forward indefinitely. Approximately \$1,100,000 of the net operating loss carryforwards and \$610,000 of the general business credit carryforwards are limited to the net income of TOCCO. Approximately \$14.8 million of the net operating loss carryforwards are limited to the net income of ASCC.

The Company has no Saudi Arabian tax liability for its activities there.

14. 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 investment in Pioche-Ely Valley Mines, Inc. for which the related investment and equity income and losses are shown separately on the balance sheet and statement of operations, respectively. The Company has no significant corporate activities.

For 1994, 1993 and 1992, essentially all activity on the Company's consolidated statement of operations relates to the refinery operations except for equity income and losses from Pioche. The 1994 results include \$74,580 of unallocated costs recorded in general and administrative expenses related to the Saudi Arabian operations. The 1992 results include immaterial amounts of interest expense related 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.

15. RELATED PARTY TRANSACTIONS

The Company shares office facilities and certain expenses with companies owned by the chairman of the Company. At December 31, 1994, these companies did not owe any amounts to the Company. Accounts receivable from these companies aggregated approximately \$16,200 at December 31, 1993.

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 Note 10 for additional information.

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ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

16. SUBSEQUENT EVENT

On March 27, 1995, the board of directors approved a Letter of Agreement between the Company and Carlyle SEAG ("Carlyle"), whereby Carlyle has been retained as the Company's financial advisor in connection with the Al Masane mining project. Carlyle's services will include, but not be limited to, (1) advising on the capitalization structure of the proposed Saudi company to be established for the project; (2) the raising of capital funds for the project implementation; and (3) assisting the Company in the filing of all licenses and necessary documents for regulatory purposes. In addition to compensation for their services, including the grant of an option allowing Carlyle to purchase 2,000,000 shares of the Company's common stock at \$1 per share, Carlyle will nominate one member to the board of directors at the Company's next board meeting and will nominate a second board member upon the closing of the financing for the Al Masane project.

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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

Oliver W. Hammonds
Attorney-at-Law

Dallas, Texas

Harb S. Al Zuhair
Chairman and Chief Executive Officer
TETRAD Development Co. Ltd.
Riyadh, Saudi Arabia
(Investments)

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

Drew Wilson
Secretary/Treasurer

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

TRANSFER AGENT AND REGISTRAR

KeyCorp Shareholder Services, Inc.

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.

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| <PP&E> | 5,440,208 |
| <DEPRECIATION> | 2,187,256 |
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| <OTHER-SE> | 19,527,542 |
| <TOTAL-LIABILITY-AND-EQUITY> | 41,056,776 |
| <SALES> | 17,564,226 |
| <TOTAL-REVENUES> | 17,764,983 |
| <CGS> | 13,750,750 |
| <TOTAL-COSTS> | 15,459,357 |
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| <LOSS-PROVISION> | 0 |
| <INTEREST-EXPENSE> | 347,364 |
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| <INCOME-TAX> | 39,973 |
| <INCOME-CONTINUING> | 2,314,129 |
| <DISCONTINUED> | 0 |
| <EXTRAORDINARY> | 578,150 |
| <CHANGES> | 0 |
| <NET-INCOME> | 2,852,306 |
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| <EPS-DILUTED> | .14 |

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