

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D. C. 20549

(Mark One)

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, 1996

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
(State or other jurisdiction of
incorporation or organization)

75-1256622
(I.R.S. Employer
Identification No.)

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

75231
(Zip Code)

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 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 17, 1997: 20,656,494.

The aggregate market value on March 17, 1997 of the registrant's voting securities held by non-affiliates was \$23,269,688.

DOCUMENTS INCORPORATED BY REFERENCE

- (a) Selected portions of the registrant's Annual Report to Stockholders for the year ended December 31, 1996.
- Parts II and IV
- (b) Selected portions of the registrant's definitive Proxy Statement for the Annual Meeting to be held May 5, 1997.
- Part III

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. 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.

The Company holds a mining lease covering a 44 square kilometer area in the Al Masane area in southwestern Saudi Arabia. In a 1996 update to the 1994 full bank feasibility study of the Al Masane lease area conducted by an independent mining consulting firm, the consultants estimate the total capital costs of the Al Masane project to be \$88.6 million. The Company will diligently pursue the financing of the project so that commercial production can begin as contemplated in the updated feasibility study. There can be no assurance that adequate capital for the project can be obtained in order for commercial production to begin as contemplated. The ultimate recovery of mineral exploration and development costs of the Company's other mineral properties cannot presently be determined.

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

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. National Mining Company, a private Saudi company ("National Mining"), which previously had a 50% interest in the joint venture formed to explore and develop the Al Masane area, relinquished its rights to the mining lease and assigned them to the Company.

The Company was granted exploration licenses for the Wadi Qatan and Jebel Harr areas in southwestern Saudi Arabia, approximately 30 kilometers east of the Al Masane area, in 1971 and 1977, respectively. The exploration licenses by their terms have expired, and although Saudi Arabian government officials have orally advised the Company that the licenses will be extended as long as mineral exploration is being carried out on the areas which they cover, formal extensions from the government have not been obtained and there can be no assurance that the Company's license rights will be honored. Although the exploration licenses were awarded jointly to the Company and National Mining, the exploration work on the license areas has been carried on exclusively by the Company. Pursuant to an agreement among the Company, National Mining and the Petroleum and Mineral Organization ("Petromin"), the official mining and petroleum company of the Saudi Arabian government, which governed the rights of the parties if an exploration license was converted into a mining lease, National Mining's rights in these jointly held expired exploration licenses entailed responsibilities of joint exploration expenditures which National Mining did not want to assume. For this reason, National Mining has orally advised the Company that it has relinquished its rights in all other areas in Saudi Arabia and assigned them to the Company. No consideration was paid by the Company to National Mining for the relinquishment of National Mining's rights in all other areas of Saudi Arabia. The Company remains a party to the agreement with Petromin notwithstanding National Mining's relinquishment of its rights. When financing for the Al Masane project is completed, the Company plans to make an application for an expanded exploration license for an area of approximately 2,800 square kilometers which includes the original Greater Al Masane area and the Wadi Qatan and Jebel Herr areas. See Item 2. Properties.

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In May 1993, the Company had discussions with Chevron Chemical Company regarding the Company's proposal to purchase 5,000 barrels per day of mixed pentanes from an Aromax(R) petrochemical project to be built in Jubail, Saudi Arabia by Chevron Chemical in a joint venture with Saudi Venture Capital Group (SVCS). The Company and some Saudi partners, all of whom are directors and/or stockholders of the Company, plan to form a Saudi limited liability company which will build and manage a processing plant located next to the Aromax(R) plant in Saudi Arabia. The Company would have a 25% interest in the limited liability company and would manage the plant. The plant will be similar to the South Hampton refinery in producing purified pentanes from a feedstock of mixed pentanes obtained from the Aromax(R) plant. Chevron Chemical advised the Company by letter in July 1993 that Chevron Chemical and SVCS have jointly agreed to commit to supply the proposed pentane project with up to 5,000 barrels per day of mixed pentane feedstock. Engineering and marketing studies of the project made in 1994 by outside consultants reflected positive results. Planning then began toward the construction and operation of the Aromax(R) plant and the processing plant but was delayed during 1995 because of the absence of a firm commitment for the feedstock supply to the Aromax(R) plant. The Aromax(R) plant received final approval from the Saudi Arabian government in March 1996 and the Company and its Saudi partners, following the confirmation of their agreement with Chevron Chemical, are preparing an application for an industrial license from the Ministry of Industry to build the processing plant. The application will be submitted in the near future.

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

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

United States Activities. The Company has two direct wholly owned subsidiaries, American Shield Refining Company (the "Refining Company") and American Shield Coal Company (the "Coal Company"). The Refining Company owns all of the capital stock of Texas Oil and Chemical Co. II, Inc. ("TOCCO"). TOCCO owns all of the capital stock of South Hampton, and South Hampton owns all of the capital stock of Gulf State Pipe Line Company, Inc. ("Gulf State"). South Hampton owns and operates a special products refinery near Silsbee, Texas. Gulf State owns and operates three pipelines which connect the South Hampton refinery to a natural gas line, to South Hampton's truck and rail loading terminal and to a marine terminal owned by an unaffiliated third party. The Company also beneficially owns approximately 55%, and directly owns approximately 46%, of the capital stock of an inactive Nevada mining company, Pioche-Ely Valley Mines, Inc. ("Pioche").

Al Masane Project

Prior Feasibility Studies. In the years following the granting of the exploration licenses in August 1971, substantial geological and geophysical work was accomplished on the Al Masane and Wadi Qatan license areas. Core drilling on the licensed areas and studies conducted by independent consulting firms indicated that the copper, zinc, gold and silver prospects at Al Masane had a chance of being put into production sooner than the nickel prospect at Wadi Qatan. Metallurgical tests also showed difficulty in separating the nickel at Wadi Qatan. During 1977, a pre-feasibility mining study was conducted at Al Masane by the mining consulting firm of Watts, Griffis and McOuatt of Toronto, Canada ("WGM"). WGM concluded that the Al Masane prospect should be further developed and recommended an extensive development program for the area.

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

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

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

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

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

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

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

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<TABLE>
<CAPTION>

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

</TABLE>

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

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

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

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

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

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

be 34,900 tonnes of copper concentrate (25% copper per tonne) containing

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

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

WGM prepared an economic analysis of the project utilizing cash flow projections. 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.

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

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

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

The base case assumes the corporate structure of the entity to be formed to operate the project, currently planned to be a Saudi limited liability company, will be owned 50% by the Company and 50% by Saudi Arabian investors and that the owners of this entity would contribute an aggregate of \$21.2 million to the cost of the project. The base case further assumes financing for the project from commercial loans in the aggregate amount of \$21.2 million bearing interest at the rate of 8% per year and a loan in the amount of \$43.8 million from the Saudi Industrial Development Fund ("SIDF") repayable in equal annual installments

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over the initial life of the mine. The remainder of the project financing would be contributed by cash generated by the operation of the project. The base case assumes that the \$11 million loan outstanding to the Saudi Arabian government will be paid by the Company in accordance with a repayment schedule to be agreed upon with the Saudi Arabian government. Based on these assumptions, and assuming the average prices of metal over the life of the mine to be \$1.05 per pound for copper, \$.60 per pound for zinc, \$400 per ounce of gold and \$6.00 per ounce of silver, WGM's economic analysis of the base case

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

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

To assist the Company in obtaining financing for the project, on March 27, 1995, the Company retained Carlyle SEAG of Washington, D.C. ("Carlyle") as the Company's financial advisor. On March 13, 1996, the agreement with Carlyle was terminated by mutual consent after Carlyle informed the Company that it had to withdraw as the Company's financial advisor because of a conflict of interest since the Carlyle Group, which owns Carlyle, advises the Saudi Arabian government on its offset program.

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

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

The agreement provides that the Saudi Arabian advisors are solely responsible for the performance of the foregoing obligations and that the Company has no obligation therefor.

As consideration for performing these obligations, the Company has agreed to pay Mr. Kadasah and Dar Al Khaleej \$10,000 each upon the issuance of the industrial license and Mr. Kadasah \$10,000 upon approval of the loan by the SIDF. The Company has also agreed to issue to Mr. Kadasah and Mr. Tawfiq

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Abdulaziz Al-Sowailim, as agent for Dar Al Khaleej, up to 1,025,000 and 975,000 shares of the Company's Common Stock, respectively, and to grant Mr. Kadasah and Mr. Tawfiq Abdulaziz Al-Sowailim, as agent for Dar Al Khaleej, options to purchase up to 1,425,000 and 875,000 shares of the Company's Common Stock, respectively. The Company is obligated to issue such shares and grant such options in designated amounts upon completion of each of the foregoing obligations. The issuance of the shares would be for consideration consisting solely of services rendered to the Company. The options are immediately exercisable on the date of grant, have a five-year term commencing on the date of formation of the Saudi limited liability company and an exercise price of \$1.00 per share.

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

Pursuant to the mining lease agreement, when the profitability of the project is established, the Company is obligated to form a Saudi public stock company with Petromin. 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. Title to the mining lease and the other obligations specified in the mining lease will be transferred to the Saudi public stock company. Responsibility for the repayment of the \$11 million loan from the Saudi Arabian government will remain with the Company. In December 1994, the Company received instructions from the office of the Minister of Petroleum and Mineral Resources stating that it is possible for the Company to form the Saudi public stock company without Petromin but that the sale of stock to the Saudi public could occur only after two years of profits from commercial operations of the mine. The instructions added that Petromin will still have the right to purchase shares in the Saudi public stock company any time it desires.

As the holder of the Al Masane mining lease, the Company is solely responsible to the Saudi Arabian government for the rental payments and other obligations provided for by the mining lease and repayment of the \$11 million loan jointly secured by the Company and National Mining from the Saudi Arabian government. The mining lease provides that the Company will repay the loan in accordance with a repayment schedule to be agreed upon with the Saudi Arabian government. The initial term of the lease is for a period of thirty (30) years from May 22, 1993, with the Company having the option to renew or extend the term of the lease for additional periods not to exceed twenty (20) years. Under the lease, the Company agreed to pay in advance a surface rental at the rate of ten thousand Saudi Riyals (approximately \$2,667 at the current exchange rate) per square kilometer per year (approximately \$117,300 annually) during the period of the lease. The Company made the rental payments for the first year of the lease. As of December 31, 1996, the Company has not paid for rentals of approximately \$309,000. It is contemplated that responsibility for the payment of these arrearages and all future rental payments would be assumed by the Saudi limited liability company when title to the Al Masane mining lease is transferred to it. In addition, the Company must pay income tax in accordance with the income tax laws of Saudi Arabia then in force and pay all infrastructure costs. Under the Saudi Arabian Mining Code, income tax will not be due during the first stage of mining operations, which is the period of five years starting from the earlier of (a) the date of the first sale of products or (b) the beginning of the fourth year since the issue of the mining lease. The lease gives the Saudi Arabian government priority to purchase the Company's whole production of gold or any part thereof from the project. The lease also gives the Saudi Arabian government the right to purchase up to 10% of the Company's annual production of other minerals on the same terms and conditions then available to other similar buyers and at current prices then prevailing in the free market. The lease contains provisions requiring that preference be given to Saudi Arabian suppliers and contractors and that the Company employ Saudi Arabian citizens and provide training to Saudi Arabian personnel.

Reference is made to the map on page 12 of this Report for information concerning the location of the Al Masane project.

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Other Exploration Areas in Saudi Arabia

During the course of the exploration and development of the Al Masane area, the Company has carried on exploration work in other areas in Saudi Arabia and is planning to apply for an additional exploration license for these areas. With respect to these other areas, the Company has an agreement with Petromin which governs the rights of the parties if the exploration licenses granted to the Company are converted into a mining lease. Under this agreement, Petromin is granted an option to acquire, at any time, a 25% interest in any project to mine minerals in Saudi Arabia the exploration for which has been conducted under exploration licenses originally granted to the Company and National Mining. National Mining has relinquished its rights in these areas and assigned them to the Company.

U.S. Mineral Interests

The Company's mineral interests in the United States include its equity interest in Pioche and the Coal Company. The Coal Company no longer owns or holds any mineral interests and is presently inactive. Pioche is also presently inactive. The future of the Coal Company's and Pioche's operations is uncertain.

Special Products Refinery

South Hampton owns and operates a special products refinery near Silsbee, Texas and currently employs 51 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(R) unit; (6) an aldehyde hydrogenation unit; and (7) a specialty fractionation unit. All of these units are presently in operation.

The design capacity of the pentane-hexane unit is approximately 2,200 BPD of feedstock. The unit averaged 1,895 barrels per stream day during 1996. 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 an aromatics extraction unit, as well as hydrogen which is utilized in other processes. The design capacity of the reformer is 4,000 BPD. The unit is operated as a source of hydrogen for the pentane-hexane unit and operates in tandem with the Aromax(R) unit as feedstock balances dictate. The unit averaged 385 barrels per stream day during 1996.

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

The cyclopentane unit consists of three specialized fractionation towers designed to produce a consistently high quality product which is used in the expandable polystyrene industry. The design capacity of the cyclopentane unit is 400 BPD. The unit operates according to the feedstock supplied by the pentane-hexane unit and averaged 190 barrels per stream day during 1996.

The Aromax(R) unit is the world's first commercial unit using a proprietary process of Chevron Research Company to produce a high benzene content product which is sold as feedstock to refiners operating benzene extraction units. The process converts petroleum naphtha into liquid hydrocarbons having a higher aromatic hydrocarbon content. The aromax unit capacity is 400 BPD and uses a by-product of the pentane-

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hexane unit as feedstock. The unit operates according to the feedstock supplied from the pentane-hexane unit and the other hydrotreaters. The unit averaged throughput of 150 barrels per stream day during 1996. Chevron Research has agreed to continue development of the Aromax(R) process. The unit has continued to successfully operate as designed.

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

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

As a result of an expansion program of the production capacity of the South Hampton refinery completed in 1990, essentially all of the standing equipment at South Hampton is operational. The Company has surplus equipment in storage on site with which to assemble further processing units, such as a hydrocracking unit with a 2,000 BPD capacity.

In January 1996, Gulf State acquired an additional five miles of natural gas pipeline and now owns and operates three 8" pipelines aggregating approximately 50 miles in length which connect the South Hampton refinery to a natural gas line, to South Hampton's truck and rail loading terminal and to a marine terminal owned by an unaffiliated third party. South Hampton leases storage facilities at the marine terminal.

Revenues and Financing

With the exception of revenues generated by the operations of the refinery, 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 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 at \$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.

In 1995, the Company (1) negotiated an extension until April 30, 1996 of the maturity of the Amended and Restated Credit Agreement with Den norske Bank AS, (2) borrowed \$721,000 in the aggregate from four individuals, including a stockholder of the Company who is the Vice Chairman of National Mining Company, a stockholder of the Company, the President and Chief Executive Officer of the Company and a relative of such executive officer, pursuant to loans payable on demand two years after their issuance bearing interest at LIBOR plus 2%, such lenders having the option for a period of five years from the date of the loan to convert the principal amount of the loan and all accrued interest into shares of the Company's Common Stock at the rate of \$1.00 per share, (3) received \$50,000 payment on a stockholder receivable from a 1993 sale of shares of its Common Stock to a private Saudi company controlled by a director and (4) granted the President and

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Chief Executive Officer of the Company an option to convert at any time \$400,000 of deferred compensation for services rendered to the Company into shares of the Company's Common Stock at the rate of \$1.00 per share.

In 1996, the Company (1) through South Hampton negotiated an Amended and Restated Credit Agreement with Den norske Bank ASA, amending and restating the then outstanding credit agreement to provide for a revolving credit facility in an aggregate principal amount of up to \$1,965,000, (2) restructured certain indebtedness of South Hampton owed to Saudi Fal Co., Ltd., a limited liability company owned by a stockholder of the Company ("Saudi Fal"), and the Refining Company pursuant to promissory notes in the original principal amounts of \$1,945,773.49 and \$1,694,605.08, respectively, which promissory notes are subordinated to the Amended and Restated Credit Agreement with Den norske Bank ASA, (3) approved the sale of up to 1 million shares of the Company's Common Stock through private placements at a price no less than \$1.00 per share, (4) sold 450,000 shares of the Company's Common Stock at \$1.00 per share to a Saudi Arabian investor who is a stockholder of the Company and approved the sale of an additional 450,000 shares of the Company's Common Stock at \$1.00 per share to the same investor, the purchase price for such additional shares being payable in monthly installments of \$100,000 and (5) approved the sale of 50,000 shares of the Company's Common Stock to a Saudi Arabian investor.

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

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

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

The refinery had operating income of approximately \$655,000, before depreciation and amortization of approximately \$413,000, on gross refined product sales of approximately \$21,367,000 for the 1996 fiscal year compared with operating income of approximately \$916,000, before depreciation and amortization of approximately \$396,000, on gross refined product sales of approximately \$17,742,000 for the 1995 fiscal year, and operating income of approximately \$3,395,000, before depreciation and amortization of \$366,000, on gross refined product sales of approximately \$17,564,000 for the 1994 fiscal year.

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

In the case of the Al Masane project, the Company must secure the financing and construction of the mining and milling facilities before revenues from that project may be realized. The 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 intends to conduct limited exploration of the Pioche properties when funds are available.

The Company believes that acceptable financing for the estimated cost of the Al Masane project can be arranged, although there can be no assurance that such financing could be obtained. The results of the 1996 update to the 1994 feasibility study show the estimated total capital costs of the project to be \$88.6 million.

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, Jr., 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 28, consist of the office personnel and field crews conducting core drilling and other exploration activities in Saudi Arabia under the supervision of Mr. Hatem El-Khalidi, President and Chief Executive Officer of the Company. South Hampton currently employs 51 persons.

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 has applied for a license covering an area surrounding the Al Masane mining lease area, which is referred to as the Greater Al Masane area. The Company and National Mining had previously made a joint application for a license for this area. If the exploration license for the Greater Al Masane area is granted, it will be owned solely by the Company. Although a license has not been formally granted for the Greater Al Masane area, the Company was authorized in writing by the Saudi Arabian government to carry out exploration work on the area. Exploration work has been carried on and paid for exclusively by the Company.

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

Reference is made to the map on page 12 of this Report for information concerning the location of the foregoing areas.

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

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

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

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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. An exploration license which includes the Wadi Qatan and Jebel Harr areas will enable the Company to continue its drilling program to prove enough ore for a viable mining operation. Although the indications are encouraging there is no assurance that a viable mining operation could be established.

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

locations. Geological, geochemical and geophysical work on the Greater Al Masane area has disclosed mineralization similar to that discovered at Al Masane.

Refining Operations

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

Nevada Mining Properties

There are 48 patented and 84 unpatented claims totaling approximately 3,700 acres in the Pioche properties. All the claims are located in the Pioche District, Lincoln County, in southeastern Nevada. There are prospects and mines on these claims which formerly produced silver, gold, lead, zinc and copper. The ore bodies are both oxidized and sulfide deposits, classified into three groups: fissure veins in quartzite, mineralized granite porphyry and replacement deposits in carbonate rocks (limestone and dolomites). The Company intends to conduct limited exploration when funds are available.

There is a 300-ton-a-day processing mill on property owned by Pioche. The mill is not currently in use and a significant expenditure would be required in order to put the mill into continuous operation. A lease of the Wide Awake mine property terminated on December 31, 1996.

Colorado Coal Properties

The Coal Company had a net operating loss carryforward of approximately \$5.9 million at December 31, 1996 which is limited to any future net income. The Company has had negotiations with several companies toward the possible use of the Coal Company's carryforward amount, but no agreements have been 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.

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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 would 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 in 1994. The court ruled in favor of National Union on July 29, 1996. No further action is planned by South Hampton in this matter.

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 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 entered into a settlement agreement with one of the plaintiffs on March 13, 1997, by agreeing to pay such plaintiff the amount of \$45,000 in full and final settlement of all claims by such plaintiff against South Hampton. South Hampton intends to vigorously defend against the remaining lawsuit.

In mid-1993, while remediating a small spill area, the Texas Natural Resources Conservation Commission ("TNRCC") requested South Hampton to drill a well to check the groundwater under the spill area. The well disclosed a pool of hydrocarbons on top of the groundwater under the truck loading rack area.

An analysis of the material indicated that the hydrocarbons were produced more than fifteen years ago when the refinery was in the business of processing crude oil. Consulting engineers were hired to determine the size and location of the pool. Monitoring wells were drilled around the perimeter of the refinery property and it was determined that there was no migration of hydrocarbons off the refinery's property. Two large pools of hydrocarbons were located, one under South Hampton's historic refinery site and the other under a neighboring property which was purchased from an independent gas producer in 1981. The acquired property had previously been the site of a natural gas processing plant. 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 was completed and approved in November 1995. The costs through 1996 for this problem totaled approximately \$153,500. Estimated costs of \$60,000 were accrued as of December 31, 1996 to cover the recovery and remediation activity expected to take place in 1997.

In November 1996, South Hampton agreed to a proposed settlement with the TNRCC's Air Permit Section for various alleged violations identified during the 1991 through 1994 inspections. An agreed fine of \$50,000 will be paid over a period of ten months, \$15,000 of which was paid in 1996 and the balance of which was accrued as of December 31, 1996. South Hampton vigorously denied many of the allegations in the settlement document, but determined that further protest of the TNRCC's interpretation and application of the rules would result in higher expenses.

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On May 15, 1991, the Company filed a complaint with the U.S. Department of Justice ("DOJ") against Hunt Oil Company of Dallas, Texas ("Hunt"), alleging violations of the Foreign Corrupt Practices Act ("FCPA") by Hunt in obtaining its Petroleum Production Sharing Agreement ("PSA") in Yemen in 1981, subsequent to the Company presenting a bid to the Yemen government for the same area before Hunt made its application. The Company's Washington, D.C. attorneys opined that, because the PSA of Hunt is still ongoing, and under its auspices, payments and receipts occur daily, the DOJ still has jurisdiction to continue its investigation. A letter from the DOJ on December 19, 1995 stated its interest in receiving additional documentation regarding the Company's allegations. On February 28, 1996, the Company sent more documents to the DOJ which it believed further supported its allegations. The Company's Washington, D.C. attorneys opined also that the Victim Restitution Act provides for restitution to the Company of monies lost as a result of the alleged wrongdoing by Hunt, if Hunt is convicted under the FCPA. A letter from the DOJ dated October 1, 1996 stated that the documents presented did not suggest any criminal events occurred within the statute of limitations, and that, at that time, the DOJ did not intend to pursue the investigation. On November 18, 1996, legal counsel retained by the Company, after studying the facts of the case, sent the DOJ an analysis concluding that while the statute of limitations of FCPA may have lapsed, the statute of limitations for conspiracy to violate the FCPA had not lapsed, and that, as a consequence, the DOJ could criminally prosecute Yemen Hunt for conspiracy to violate the FCPA. The Company's legal counsel met with the Fraud Section of the DOJ on December 13, 1996 and were told that the DOJ would take a more aggressive stance if more information of evidentiary quality were presented to the DOJ. The Company intends to vigorously pursue obtaining such further information in the United States and in Yemen.

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

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

No matter was submitted to a vote of the Company's stockholders during the fourth quarter of 1996.

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 1996 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, 1996, of the Company's 1996 Annual Report to Stockholders filed herein as Exhibit 13, which portion of such Annual Report is incorporated herein by reference.

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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 1996 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 1996 Annual Report to Stockholders filed herein as Exhibit 13, are incorporated herein by reference.

Item 9. Disagreements on Accounting and Financial Disclosure.

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

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PART III

Item 10. Directors and Executive Officers of the Registrant.

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

Item 11. Executive Compensation.

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

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

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

Item 13. Certain Relationships and Related Transactions.

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

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

- (a) 1. The following financial statements are incorporated by reference from the Company's 1996 Annual Report to Stockholders filed herein as Exhibit 13:
- Reports of Independent Accountants.
Consolidated Balance Sheets dated December 31, 1996 and 1995.
Consolidated Statement of Operations for the three years ended December 31, 1996.
Consolidated Statement of Stockholders' Equity for the three years ended December 31, 1996.
Consolidated Statement of Cash Flows for the three years ended December 31, 1996.
Notes to Consolidated Financial Statements.
2. The following financial statement schedules are filed with this Report:
- Schedule II - Valuation and Qualifying Accounts for the three years ended December 31, 1996.
3. The following documents are filed or incorporated by reference as exhibits to this Report:
- 3(a) Certificate of Incorporation of the Company as amended through the Certificate of Amendment filed with the Delaware Secretary of State on January 29, 1993 (incorporated by reference to Exhibit 3(a) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
- 3(b) Bylaws of the Company, as amended through July 6, 1994 (incorporated by reference to Exhibit 3(b) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
- 10(a) Contract dated July 29, 1971 between the Company, National Mining Company and Petromin (incorporated by reference to Exhibit 10(a) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
- 10(b) Loan Agreement dated January 24, 1979 between the Company, National Mining Company and the Government of Saudi Arabia (incorporated by reference to Exhibit 10(b) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).

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

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

- 10(e) 1987 Non-Employee Director Stock Plan (incorporated by reference to Exhibit 10(f) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
 - 10(f) Phantom Stock Plan of Texas Oil & Chemical Co. II, Inc. (incorporated by reference to Exhibit 10(g) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
 - 10(g) Agreement dated March 10, 1988 between Chevron Research Company and South Hampton Refining Company, together with related form of proposed Contract of Sale by and between Chevron Chemical Company and South Hampton Refining Company (incorporated by reference to Exhibit 10(o) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
 - 10(h) Addendum to the Agreement Relating to AROMAX(R) Process - Second Commercial Demonstration dated June 13, 1989 by and between Chevron Research Company and South Hampton Refining Company (incorporated by reference to Exhibit 10(p) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
 - 10(i) Vehicle Lease Service Agreement dated September 28, 1989 by and between Silsbee Trading and Transportation Corp. and South Hampton Refining Company (incorporated by reference to Exhibit 10(q) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
 - 10(j) Letter Agreement dated May 3, 1991 between Sheikh Kamal Adham and the Company (incorporated by reference to Exhibit 10(t) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
 - 10(k) Promissory Note dated February 17, 1994 from Hatem El-Khalidi to the Company (incorporated by reference to Exhibit 10(u) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
 - 10(l) Letter Agreement dated August 15, 1995 between Hatem El-Khalidi and the Company (incorporated by reference to Exhibit 10(v) to the Company's Annual Report on Form 10-K for the year ended December 31, 1995 (File No. 0-6247)).
 - 10(m) Letter Agreement dated August 24, 1995 between Sheikh Kamal Adham and the Company. (incorporated by reference to Exhibit 10(w) to the Company's Annual Report on Form 10-K for the year ended December 31, 1995 (File No. 0-6247)).
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- 10(n) Letter Agreement dated October 23, 1995 between Sheikh Fahad Al-Athel and the Company (incorporated by reference to Exhibit 10(x) to the Company's Annual Report on Form 10-K for the year ended December 31, 1995 (File No. 0-6247)).
 - 10(o) Letter Agreement dated December 6, 1995 between Ibrahim Khalidi and the Company (incorporated by reference to Exhibit 10(y) to the Company's Annual Report on Form 10-K for the year ended December 31, 1995 (File No. 0-6247)).
 - 10(aa) Amended and Restated Credit Agreement dated October 15, 1996 between South Hampton Refining Company and Den norske Bank ASA, together with related Promissory Note, Ratification of Security Agreement, Ratification of Pledge Agreement, Ratification of Assignment of Insurance,

Subordination Agreement, Termination Agreement, Ratification of Subordination Agreement, Renewal, Extension and Modification Agreement, Second Lien Promissory Note and Third Lien Promissory Note of even date therewith.

- 10(bb) Letter Agreement dated November 30, 1996 between Sheikh Fahad Al-Althel and the Company.
- 10(cc) Financial and Legal Services and Advice Agreement dated May 20, 1996 by and among Nasir Ali Kadasah, Dar Al Khaleej and the Company, as amended by Letter Agreement dated March 3, 1997.
- 13 1996 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 1996 Annual Report to Stockholders is not to be deemed filed as part of this Report.
- 21 Subsidiaries (incorporated by reference to Exhibit 21 to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
- 27 Financial Data Schedule.

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

Current Report on Form 8-K dated December 24, 1996.

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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 28, 1997

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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 28, 1997.

Signature

Title

<p>----- /s/ HATEM EL-KHALIDI ----- Hatem El-Khalidi</p>	President, Chief Executive Officer and Director (principal executive officer)
<p>----- /s/ DREW WILSON, JR. ----- Drew Wilson, Jr.</p>	Secretary and Treasurer (principal financial and accounting officer)
<p>----- /s/ JOHN A. CRICHTON ----- John A. Crichton</p>	Chairman of the Board and Director
<p>----- /s/ OLIVER W. HAMMONDS ----- Oliver W. Hammonds</p>	Director
<p>----- /s/ HARB S. AL ZUHAIR ----- Harb S. Al Zuhair</p>	Director
<p>----- /s/ MOHAMMED O. AL-OMAIR ----- Mohammed O. Al-Omair</p>	Director
<p>----- /s/ GHAZI SULTAN ----- Ghazi Sultan</p>	Director

REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS ON SCHEDULES

Board of Directors and Stockholders
Arabian Shield Development Company

In connection with our audit of the consolidated financial statements of Arabian Shield Development Company and Subsidiaries referred to in our report dated March 14, 1997, which is included in the annual report to stockholders in Part II of this Form 10-K, we have also audited Schedule II at December 31, 1996 and for the year then ended. In our opinion, this schedule presents fairly, in all material respects, the information required to be set forth therein. Our report on the financial statements referred to above includes an explanatory paragraph which discusses that there is substantial doubt about the Company's ability to continue as a going concern.

/s/ GRANT THORNTON LLP

Dallas, Texas
March 14, 1997

SCHEDULE II

Arabian Shield Development Company and Subsidiaries

VALUATION AND QUALIFYING ACCOUNTS

Three years ended December 31, 1996

<TABLE>
<CAPTION>
Description

	Beginning	Charged (credited) to earnings	Deductions	Ending balance
	-----	-----	-----	-----
<S>	<C>	<C>	<C>	<C>

ALLOWANCE FOR
DOUBTFUL ACCOUNTS - (a)

December 31, 1994	\$ 231,603	\$ 12,551	\$ --	\$ 244,154
December 31, 1995	244,154	16,092	--	260,246
December 31, 1996	260,246	27,774	--	283,020

ALLOWANCE FOR DEFERRED
TAX ASSET

December 31, 1994	11,239,774	(1,450,467)	--	9,789,307
December 31, 1995	9,789,307	2,014,440	--	11,803,747
December 31, 1996	11,803,747	179,553	(403,182) (b)	11,553,118

</TABLE>

(a) Valuation account deducted in the balance sheet from trade accounts receivable and other assets.

(b) Expiration of carryforwards

EXHIBIT INDEX

<TABLE>
<CAPTION>

EXHIBIT
NUMBER

DESCRIPTION

<S>	<C>
3(a)	Certificate of Incorporation of the Company as amended through the Certificate of Amendment filed with the Delaware Secretary of State on January 29, 1993 (incorporated by reference to Exhibit 3(a) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
3(b)	Bylaws of the Company, as amended through July 6, 1994 (incorporated by reference to Exhibit 3(b) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0- 6247)).
10(a)	Contract dated July 29, 1971 between the Company, National Mining Company and Petromin (incorporated by reference to Exhibit 10(a) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
10(b)	Loan Agreement dated January 24, 1979 between the Company, National Mining Company and the Government of Saudi Arabia (incorporated by reference to Exhibit 10(b) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
10(c)	Mining Lease Agreement effective May 22, 1993 by and between the Ministry of Petroleum and Mineral Resources and the Company, together with English translation thereof (incorporated by reference to Exhibit 10(d) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
10(d)	Stock Option Plan of the Company, as amended (incorporated by reference to Exhibit 10(e) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
10(e)	1987 Non-Employee Director Stock Plan (incorporated by reference to Exhibit 10(f) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).

</TABLE>

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<S>	<C>
10(f)	Phantom Stock Plan of Texas Oil & Chemical Co. II, Inc. (incorporated by reference to Exhibit 10(g) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0- 6247)).

10(g)	Agreement dated March 10, 1988 between Chevron Research Company and South Hampton Refining Company, together with related form of proposed Contract of Sale by and between Chevron Chemical Company and South Hampton Refining Company (incorporated by reference to Exhibit 10(o) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
10(h)	Addendum to the Agreement Relating to AROMAX(R) Process -Second Commercial Demonstration dated June 13, 1989 by and between Chevron Research Company and South Hampton Refining Company (incorporated by reference to Exhibit 10(p) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
10(i)	Vehicle Lease Service Agreement dated September 28, 1989 by and between Silsbee Trading and Transportation Corp. and South Hampton Refining Company (incorporated by reference to Exhibit 10(q) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0- 6247)).
10(j)	Letter Agreement dated May 3, 1991 between Sheikh Kamal Adham and the Company (incorporated by reference to Exhibit 10(t) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
10(k)	Promissory Note dated February 17, 1994 from Hatem El-Khalidi to the Company (incorporated by reference to Exhibit 10(u) to the Company's Quarterly Report on Form 10-Q/A for the quarter ended September 30, 1994 (File No. 0-6247)).
10(l)	Letter Agreement dated August 15, 1995 between Hatem El-Khalidi and the Company (incorporated by reference to Exhibit 10(v) to the Company's Annual Report on Form 10-K for the year ended December 31, 1995 (File No. 0-6247)).
10(m)	Letter Agreement dated August 24, 1995 between Sheikh Kamal Adham and the Company. (incorporated by reference to Exhibit 10(w) to the Company's Annual Report on Form 10-K for the year ended December 31, 1995 (File No. 0-6247)).
</TABLE>	
<TABLE>	
<S>	
10(n)	<C> Letter Agreement dated October 23, 1995 between Sheikh Fahad Al-Athel and the Company (incorporated by reference to Exhibit 10(x) to the Company's Annual Report on Form 10-K for the year ended December 31, 1995 (File No. 0-6247)).
10(o)	Letter Agreement dated December 6, 1995 between Ibrahim Khalidi and the Company (incorporated by reference to Exhibit 10(y) to the Company's Annual Report on Form 10-K for the year ended December 31, 1995 (File No. 0-6247)).
10(aa)	Amended and Restated Credit Agreement dated October 15, 1996 between South Hampton Refining Company and Den norske Bank ASA, together with related Promissory Note, Ratification of Security Agreement, Ratification of Pledge Agreement, Ratification of Assignment of Insurance, Subordination Agreement, Termination Agreement, Ratification of Subordination Agreement, Renewal, Extension and Modification Agreement, Second Lien Promissory Note and Third Lien Promissory Note of even date therewith.
10(bb)	Letter Agreement dated November 30, 1996 between Sheikh Fahad Al-Althel and the Company.
10(cc)	Financial and Legal Services and Advice Agreement dated May 20, 1996 by and among Nasir Ali Kadasah, Dar Al Khaleej and the Company, as amended by Letter Agreement dated March 3, 1997.
13	1996 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 1996 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>

AMENDED AND RESTATED

CREDIT AGREEMENT

for an amount of

up to

USD 1,965,000.00

to

SOUTH HAMPTON REFINING COMPANY

provided by

DEN NORSE BANK ASA

I N D E X

<TABLE>

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- Exhibit A - Form of Promissory Note
- Exhibit B - Form of Borrowing Base Certificate
- Exhibit C-1 - Form of Administrative Distribution Report
- Exhibit C-2 - Form of Interest Distribution Report
- Exhibit C-3 - Form of Excess Distribution Report

Amended and Restated Credit Agreement dated October 15, 1996 (the "Restated Agreement") between South Hampton Refining Company, a Texas corporation (the "Borrower") and Den norske Bank ASA, New York Branch, a Norwegian bank (the "Bank").

WHEREAS, the Borrower and the Bank entered into the Credit Agreement dated March 3, 1988 as amended and restated from time to time (as so amended and restated, the "Credit Agreement"); and

WHEREAS, the Credit Agreement was entered into for the purpose of financing, renewing and extending the Old Loan as defined in the Credit Agreement; and

WHEREAS, the Borrower and the Bank wish to amend and restate the Credit Agreement to modify certain provisions of the Credit Agreement and to embody all of the amendments made to the Credit Agreement in one document.

NOW, THEREFORE, in consideration of the above recitals and other good and valuable consideration, the receipt and sufficiency of which is hereby acknowledged, the parties hereto agree to amend and restate the Credit Agreement to read in its entirety as follows:

1. DEFINITIONS

"USD"	means the lawful currency of the United States of America.
"Administrative Distribution"	means a distribution by the Borrower to a Parent Company in respect of legal, auditing and accounting fees of the Parent Companies attributable to the operations of Borrower.
"Advance"	means the loans by the Bank to the Borrower pursuant to Section 2 hereof.
"American Shield"	means American Shield Refining Company, a Delaware corporation.
"Arabian Shield"	means Arabian Shield Development Company, a Delaware corporation.
"Banking Day"	means a day upon which banks are open for business in such places contemplated for the transactions required by this Restated Agreement.
"Borrowing Base"	means the aggregate of (i) 90% of cash of the Borrower held in the Cash Collateral Accounts, (ii) 80% of Eligible Accounts Receivable and (iii) 60% of Inventory.
"Borrowing Base Certificate"	means a certificate in the form of Exhibit B attached hereto.
"Cash Collateral Accounts"	means the accounts at Silsbee State Bank providing for the payment of all the Borrower's receivables to a designated account or accounts under the joint control of the Borrower and the Bank.
"Closing Date"	means October 15, 1996.
"Commitment"	means an amount up to USD 1,965,000.00 on the Closing Date, reducing (i) on the last day of each fiscal quarter of the Borrower commencing December 31, 1996 by the sum of USD 75,000 and (ii) by the amount of any Distribution Reduction on the date the corresponding Distribution is made.
"Credit Facility"	means the revolving credit facility, the terms

and conditions of which are set out in Section 2 of this Restated Agreement.

"Current Ratio" means the ratio of the current assets of the Borrower to its current liabilities (excluding indebtedness to the Bank in excess of USD 300,000) as each would be classified as current assets or liabilities in accordance with generally accepted accounting principles in the U.S., of a corporation conducting a business the same as or similar to the business of the Borrower, but excluding receivables from or payables to any subsidiary, parent or affiliate of the Borrower.

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"Distribution Reduction" means an amount equal to (i) 2 times any Excess Distribution if the shareholders' equity of TOCCO II is negative or (ii) any Excess Distribution if the shareholders' equity of TOCCO II is positive.

"Eligible Accounts Receivable" means all accounts receivable which have been created in the ordinary course of Borrower's business and for which Borrower's right to receive payment is absolute and not contingent upon the fulfillment of any condition whatsoever, and shall not include (a) any invoice of a customer which remains unpaid more than 90 days from its invoice date, (b) any account for which there exists a right of set off, counterclaim, dispute, objection, complaint, defense or discount, (c) any account which arises from the sale or lease to or performance of services for, or represents an obligation of, an employee, affiliate, partner, parent or subsidiary of Borrower, (d) that portion of any account from a customer of Borrower which represents the amount by which Borrower's total accounts from such customer exceeds 25% of Borrower's total accounts, (e) any account arising from a sale or lease to a non-United States or non-Canadian customer, and (f) any account designated to Borrower by the Bank in which the Bank is not or does not continue to be, in the Bank's reasonable judgment, satisfied with the credit standing of the customer of Borrower in relation to the amount of credit extended.

"Excess Distribution" means a distribution by Borrower to a Parent Company that is not an Administrative Distribution, an Interest Distribution, a dividend or a return of capital.

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"Fixed Charge Coverage Ratio" means the ratio of (a) the earnings of the Borrower excepting extraordinary items of gain or loss, but without deduction for interest, taxes, depreciation and amortization to (b) the aggregate of scheduled payments of principal of all debt of the Borrower and interest thereon.

"Hazardous Substance" means any hazardous, dangerous or toxic waste, substance or material as defined in the Comprehensive Environmental Response, Compensation and Liability Act of 1980, 42 U.S.C.

Sec. 9601, et seq. (hereinafter, "CERCLA"); the
-- ---
Resource Conservation and Recovery Act, 42 U.S.C.
Sec. 6901, et seq. (hereinafter, "RCRA"); the
-- ---
Hazardous Materials Transportation Act, 49 U.S.C.
Sec. 1801, et seq.; the Texas Solid Waste
-- ---
Disposal Act, Tex. Rev. Civ. Stat. Ann. Art.
4777-7 Sec. 13(g)(7); or any other federal, state
or local statute, law, ordinance, code or
regulation relating to or imposing liability or
standards of conduct concerning the use,
production, generation or disposal of any
hazardous, toxic or otherwise dangerous waste,
substance, or material, currently or at any time
hereafter, in effect.

"Interest Distribution" means a payment by Borrower to a Parent Company in respect of accrued interest on any debt owed by Borrower to Saudi Fal or Arabian Shield.

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"Inventory" means any and all of Borrower's right, title and interest in and to inventory, wherever located, and in which the Bank has a perfected security interest, including without limitation, any and all goods held for sale or lease or being processed for sale or lease in Borrower's business, as now or hereafter conducted, including without limitation, all feed stock, materials, goods, and work-in-progress, finished goods, and other tangible property held for sale or lease or furnished or to be furnished under the contracts of service or used or consumed in Borrower's business, along with all documents (including documents of title) covering inventory, all cash and non-cash proceeds from the sale of inventory including proceeds from insurance and including such property the sale or other disposition of which has given rise to accounts and which has not been returned to or repossessed or stopped in transit by Borrower, but specifically excluding obsolete or slow moving inventory.

"Margin" means 1% (one percent).

"Maturity Date" means December 31, 1998 or as extended in the sole discretion of the Bank.

"Monthly Cash Flow" means a certificate in the form of Certificate Exhibit D attached hereto and made a part of this Restated Agreement for all purposes which indicates the monthly cash flow of the Borrower and the additional commitment reduction amount referred to in Section 6(ii) of this Restated Agreement.

"Parent Company" means Saudi Fal, American Shield Refining Company, Arabian Shield Development Company and Texas Oil & Chemical Co. II, or any combination thereof.

"Payment Date"	means the last day of each month during the term of this Restated Agreement.
"Permitted Distribution"	shall have the meaning set forth in Section 9(d) hereof.
"Prime Rate"	shall mean the rate announced from time to time by the Bank as its prime lending rate in effect in its New York, New York office, automatically fluctuating upward and downward with and at the time of each such announcement without special notice to Borrower or any other Person. The Bank's prime rate may be one of several interest rates, may serve only as reference rate and may not be the Bank's lowest rate.
"Saudi Fal"	means Saudi Fal, a limited liability company.
"Security Documents"	means all or any documents pursuant to Section 8 hereof, as have been or may be entered into as security for all or any of the obligations of the Borrower hereunder.
"Tax"	means all or any levies, imposts, duties, charges, fees, deductions and withholdings levied or imposed by any national or local governmental or public body or authority (except for United States federal, state and local income taxes levied on the Bank's gross income or receipts or United States federal, state and local gross receipts or franchise taxes levied in lieu of income taxes) and any restrictions or conditions resulting in a charge.
"TOCCO II"	means Texas Oil & Chemical Co. II, Inc., a Texas corporation.

Where the context of this Agreement so allows, words importing the singular include the plural and vice versa.

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2. AMOUNT AND PURPOSE

(a) The Bank shall make available the Commitment as follows:

USD 1,965,000.00 which shall be used by the Borrower for the purpose of refinancing, renewing and extending the loan evidenced by its Promissory Note dated December 30, 1990, as amended or restated from time to time (the "Old Note"); and

(b) The Commitment shall be drawn down by the Borrower in the form of Advances for a term which shall not extend beyond the Maturity Date. The total amount of Advances outstanding under the Credit Facility shall not exceed at any time the lesser of the Commitment and the Borrowing Base. Within such limit, the Borrower may borrow, prepay pursuant to Section 7 of this Restated Agreement and reborrow under this Section 2(b). Each borrowing by the Borrower shall be in an aggregate principal amount of at least USD 50,000.

(c) The Commitment shall be evidenced by the promissory note of the Borrower in the form of Exhibit A attached hereto (the "Note").

(d) Notwithstanding anything else in this Restated Agreement, at no time shall there be outstanding Advances in an amount in the aggregate greater than the lesser of the Commitment and the Borrowing Base.

3. CONDITIONS PRECEDENT

3.1 The Borrower shall give the Bank at least one Banking Day irrevocable prior written notice of its desire to have an Advance made.

3.2 The obligation of the Bank to make the first Advance under this Restated Agreement shall be subject to the Bank or its legal counsel having received in form and content satisfactory to the Bank:

(a) The counterparts of this Restated Agreement duly executed by the Borrower's authorized representative or representatives.

(b) The Security Documents.

(c) Copies certified by the Secretary of the Borrower of:

(i) the By-Laws of the Borrower,

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(ii) The resolutions of the Board of Directors of the Borrower approving the execution, delivery and performance by the Borrower of this Restated Agreement, the Note, the Security Documents and specifying the persons authorized to sign the above mentioned documents on its behalf.

(d) Any consents necessary from governmental or other authorities for the execution, delivery and performance by the Borrower of this Restated Agreement.

(e) A copy certified as of a recent date by the Secretary of State of Texas of the Articles of Incorporation of the Borrower with all amendments thereto.

(f) Evidence from the Secretary of State and the Comptroller of Public Accounts of the State of Texas as to the continued existence and good standing of the Borrower.

(g) An opinion of counsel to the Borrower acceptable to the Bank as to:

(i) the valid existence and good standing of the Borrower under the laws of the State of Texas.

(ii) the due authorization, execution and delivery by the Borrower of this Restated Agreement, the Note and the Security Documents to which it is a party.

(iii) this Restated Agreement, the Note and the Security Documents to which the Borrower is a party constituting the legally valid and binding obligations of the Borrower in accordance with their terms.

(iv) the execution, delivery and performance of this Restated Agreement, the Note and the Security Documents to which the Borrower is a party, by the Borrower not resulting in a breach of any terms or conditions of, or resulting in the imposition of any lien, charge or encumbrance upon any properties of the Borrower or constituting a default under any indenture, agreement, order, judgment or other instrument under which the Borrower or its property may be bound or constituting a violation of the Articles of Incorporation or By-Laws of the Borrower or violating any provision of applicable law.

(v) the execution, delivery and performance of this Agreement, the Note and the Security Documents to

which the Borrower is a party by the Borrower not requiring the consent or approval of, the giving of notice to, the registration with or the taking of any action by any governmental authority of the United States or the State of Texas.

(vi) such other matters as the Bank may request.

(h) the Note.

(i) Uniform Commercial Code financing statements covering the security interests granted by the Security Documents shall have been duly executed by the Borrower as debtor, and duly filed in all places as are, in the opinion of the Bank, necessary or desirable to perfect said security interest.

(j) Evidence of the insurance required by Section 9(b) (vii) hereof.

(k) An agreement pursuant to which Saudi Fal subordinates all amounts owed to it by TOCCO II and the Borrower to all amounts outstanding under this Restated Agreement and agrees that no payments of principal or interest shall be made under such loans until such time as all amounts due under this Restated Agreement have been paid, except for Permitted Distributions under Section 9(d) hereof.

(l) An acknowledgment by American Shield Refining Company and Arabian Shield Development Company of the continuing effectiveness of the subordination agreement with terms similar to those set forth in subsection (k) above.

(m) Evidence of cancellation of the Intercreditor Agreement between the Bank and Saudi Fal.

3.4 The obligations of the Bank to make each subsequent Advance shall be subject to the further condition precedent that the Bank shall have received a certificate dated the date of such Advance of the Borrower certifying that:

- (a) the representations and warranties contained in Section 9 are true and correct on and as of the date of such Advance as though made on and as of such date; and
- (b) no event has occurred and is continuing, or would result from such Advance, which constitutes an Event of Default or with the passing of time or the giving of notice would constitute an Event of Default.

3.5 All of the conditions precedent contained in this Section 3 are for the sole benefit of the Bank and the Bank may waive any of them in its absolute discretion.

4. EXTENSION RENEWAL AND AVAILABILITY

Subject to the provisions of Sections 10 and 11 hereof and:

- (a) The Bank's prior satisfaction that the relevant conditions set out in Section 3 above have been complied with,
- (b) No Event of Default as defined in Section 15 herein has occurred or is continuing,

the indebtedness evidenced by the Old Note shall be refinanced, extended, renewed and restructured and the new credit facility of Facility B shall be made available to the Borrower all in accordance with the terms and provisions of this Restated Agreement.

5. INTEREST

(a) Interest Rate

The Borrower shall pay interest on the Advances drawn and outstanding under this Restated Agreement at the annual rate which is conclusively certified by the Bank to be the aggregate of the Margin and the Prime Rate.

(b) Interest Payment

(i) Interest shall be payable monthly in arrears on the last day of each month and on the Maturity Date and calculated in accordance with Section 14 hereof.

(ii) If any interest would be payable on a non-Banking Day, it shall be paid on the next succeeding Banking Day.

(c) Computation of Interest

Notwithstanding any provision of this Restated Agreement or the Note to the contrary, in no event shall the aggregate amount of consideration which constitutes interest under any applicable law which is contracted for, charged or received hereunder or under the Note ("Interest") exceed the maximum amount of nonusurious interest allowed by law, and any excess shall be credited on this Restated Agreement or the Note (or if all obligations under this Restated Agreement or the Note shall have been paid in full, refunded to the Borrower). For purposes of the foregoing, the maximum amount of

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interest allowed by law shall be calculated by determining the amount of interest that could be contracted for, charged or received during the term hereof at the maximum rate of nonusurious interest allowed from time to time by applicable law as is now or, to the extent allowed by law, as may hereafter be in effect (the "maximum nonusurious interest rate") and, if at any time the rate of Interest to accrue would exceed the maximum nonusurious interest rate, the rate of Interest to accrue under this Restated Agreement or the Note shall be limited to the maximum nonusurious interest rate, but any subsequent reductions in LIBOR shall not reduce the rate of Interest to accrue under this Restated Agreement or the Note below the maximum nonusurious interest rate until the total amount of Interest accrued and paid under this Restated Agreement or the Note equals the amount of Interest which would have accrued if a rate per annum equal to the Prime Rate plus the Margin had at all times been in effect.

6. REPAYMENT

The Borrower shall repay all principal amounts outstanding plus any other outstanding amounts hereunder in a single installment on the Maturity Date. Subject to the terms hereof, the Borrower may reborrow amounts repaid or prepaid prior to the Maturity Date, upon one (1) day prior written notice to the Bank.

7. PREPAYMENT

The Borrower shall make an immediate prepayment in an amount by which the principal amount outstanding hereunder exceeds the Commitment or the Borrowing Base, if ever.

8. SECURITY

The Facility is secured by:

(a) The Deed of Trust dated September 10, 1985 from Texas Oil & Chemical Co. ("Chemical") to Michael E. Niebruegge as Trustee.

(b) The Deed of Trust dated January 10, 1985 from Gulf State Pipe Line Company, Inc. ("Gulf State") to Michael E. Niebruegge as Trustee.

(c) The Deed of Trust dated January 20, 1985 from the Borrower to Michael E. Niebruegge as Trustee.

(d) The Deed of Trust dated April 8, 1986 from Texas Oil & Chemical Terminal, Inc. ("Terminal") to Michael E. Niebruegge as Trustee.

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(e) The Security Agreement and Financing Statement from the Borrower to the Bank dated as of January 14, 1985, duly ratified by the Borrower.

(f) The Cash Collateral Accounts.

(g) An Assignment of Insurances dated March 3, 1988 from the Borrower, Gulf State and Texas Oil & Chemical Co. II, Inc., duly ratified by the parties thereto.

(h) A pledge by American Shield Refining Company of all of the issued and outstanding shares of Texas Oil & Chemical Co. II, Inc. in form and substance satisfactory to the Bank, duly ratified by the parties thereto.

9. REPRESENTATIONS AND COVENANTS

(a) The Borrower represents to and agrees with the Bank that:

(i) this Restated Agreement and the Security Documents to which it is a party constitute valid, binding and enforceable obligations of the Borrower according to the terms and conditions hereof and thereof and the execution and performance of this Restated Agreement and such Security Documents do not and will not contravene any applicable law, order, regulation or restriction of any kind binding on the Borrower.

(ii) the Borrower is a duly formed and validly existing corporation under the laws of the State of Texas, has full power to enter into this Restated Agreement and the Security Documents to which it is party, to make borrowings hereunder and to service and repay the Commitment.

(iii) the chief executive office of the Borrower is located at Highway 418, Silsbee, Texas.

(iv) it is currently in possession of permits authorizing all activities now or formerly conducted on the properties securing this indebtedness from the Texas Water Commission, the Texas Air Quality Control Board, the U.S. Environmental Protection Agency, the U.S. Army Corps of Engineers and the Texas Railroad Commission. Furthermore, the Borrower agrees that it maintains no Hazardous Substances on the properties securing this indebtedness without possession of the appropriate permits.

(v) no Event of Default has occurred and is continuing.

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(b) Affirmative Covenants. The Borrower undertakes to the Bank that so long as any amount is owing hereunder it will:

(i) promptly inform the Bank of any occurrence of which it becomes aware which is, or with the passage of time or the giving of notice would constitute, an Event of Default hereunder or under any of the Security Documents to which it is a party or which in its reasonable opinion might adversely affect its

ability fully to perform its obligations under this Restated Agreement or any of the Security Documents to which it is a party.

- (ii) deliver to the Bank by the 105th day of the end of the each fiscal year, consolidated annual audited financial statements, including consolidating financial statements of the Borrower, and by the 30th day after the end of each month, profit and loss and balance sheet statements.
- (iii) deliver to the Bank by the 30th day following the end of each quarter, statements showing the source and use of funds of the Borrower for the preceding quarter.
- (iv) deliver to the Bank within 3 Banking Days of the last day of each calendar month and the 15th day of each calendar month a Borrowing Base Certificate as of such days as well as a certificate signed by the President or the Chief Financial Officer of the Company as to the inventory and accounts receivable (status and aging) of the Borrower.
- (v) deliver to the Bank within 30 Banking days of the last day of each fiscal quarter, compliance statements signed by the President or Chief Financial Officer of the Borrower certifying that the Borrower is in compliance with all of the representations and covenants hereof as if made on the date of such certificate, and that no default has occurred hereunder, together with a calculation of all financial ratios set forth in Section 9(c) (ix), (x) and (xi) hereof.
- (vi) deliver to the Bank no later than December 1 of each year the business plan, income and expense projections, projected balance sheet and projected sources and uses of funds statement of the Borrower for the subsequent calendar year.
- (vii) deliver to the Bank within 30 Banking days of the end of each calendar month a written status report of the Borrower's operations, financial performance and out-

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standing accounts payable for the previous calendar month and such other financial information as the Bank may from time to time reasonably request; permit the Bank or its representative at any reasonable time or times to inspect the properties of the Borrower and to inspect, audit and examine the books or records of the Borrower and to take extracts therefrom. The Bank shall further have the right to order an audit of Borrower's books and records, no more than twice annually. The costs of such audit shall be borne by the Borrower.

- (viii) deliver to the Bank, as soon as available, weekly receipt and disbursement reports.
- (ix) maintain insurance acceptable to the Bank including, but not limited to, casualty insurance with responsible and reputable insurance companies or associations in such amounts and covering such risks as is usually carried by companies engaged in similar businesses and owning similar properties in the same general areas in which the Borrower operates. The Borrower shall furnish the Bank with evidence of all such insurance policies currently in force and with evidence of payment of the premiums on such policies.
- (x) execute and deliver to the Bank any instruments, documents or certificates which in the Bank's judgment are necessary to amend, modify, extend or supplement any of the Security Documents to better evidence, reflect and secure the Note.
- (xi) perform and maintain, or cause to be performed or maintained,

all permits, licenses, consents and agreements concerning its assets or operations.

- (xii) notify the Bank, within five (5) days, should it ever come into possession of knowledge or have a claim or complaint asserted against it because the Borrower or any other person or entity caused or permitted any Hazardous Substances to be stored, located, held or disposed of on, under or at any of the properties securing Facility A or Facility B in a manner not in compliance with all applicable laws, regulations and permits regarding such storage, holding or disposal.
- (xiii) give the Bank, within five (5) days, written notice in the event the Borrower receives notice of (1) the happening of any spill or cleanup of Hazardous Substances affecting the properties securing the Credit Facility, or

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any other property owned by the Borrower that would require the Borrower to notify any environmental agency, of any federal, state or local government of such spill or cleanup; or (2) any complaint, violation, notice or citation regarding any permit controlling the environmental health or safety violation of the Borrower, including health or safety violation of the Borrower, including without limitation, any notice from the Environmental Protection Agency.

- (xiv) indemnify and hold the Bank harmless from and against any and all claims, losses, liability, damages and injuries of any kind whatsoever incurred or suffered by or asserted against the Bank with respect to or as a direct result of the presence, escape, seepage, spillage, leaking, discharge or migration from any of the properties securing the Credit Facility of any Hazardous Substance, including without limitation, any claims asserted or arising under CERCLA, RCRA or the Texas Solid Waste Disposal Act, regardless of whether or not caused by or within the control of the Borrower.
 - (xv) cause each agreement between the Borrower and the holder of any debt subordinated to the Loan to provide that such holder may not accelerate the payment of such subordinated debt until all amounts outstanding hereunder, now or in the future, are repaid or prepaid in full.
 - (xvi) maintain its Inventory and other properties in good and safe working order. The Bank shall have the right to perform an inspection of Borrower's Inventory and properties four (4) times per year upon at least two (2) days' prior notice to the Borrower. The costs of such inspections shall be borne by the Borrower.
 - (xvii) deliver to the Bank an Administrative Distribution Report, Interest Distribution Report, or Excess Distribution Report, as the case may be, three (3) days prior to any distribution by the Borrower of the kind described in Section 9(d) hereof, each in form substantially similar to Exhibit C-1, C-2 or C-3 attached hereto, as appropriate.
- (c) Negative Covenants. The Borrower undertakes to the Bank that so long as any amount is owing hereunder it will not without the prior written consent of the Bank:
- (i) create or permit to subsist, without the prior written consent of the Bank, any mortgage, pledge, lien or other

security interest on any or all of its present or future revenues, properties or assets except liens in favor of Saudi Fal and Arabian Shield duly subordinated to any liens in favor of the Bank and liens permitted by the Security Documents or with the prior written consent of the Bank or as disclosed to the Bank in writing and accepted by the Bank on the Closing Date;

- (ii) borrow any money, enter into any lease or other financial obligation or enter into any guarantee for the obligations or the indebtedness of any third party without the prior written consent of the Bank except (1) loans or leases entered into in connection with the acquisition of equipment in the ordinary course of business, which loans or leases shall not exceed \$100,000 in the aggregate at any time and (2) one or more letters of credit issued by Silsbee State Bank, naming Vastar Resources, Inc. as beneficiary, the aggregate face amount of which shall not exceed USD 110,000;
- (iii) merge with any other entity or change its present line of business. For the purposes of this Restated Agreement, the Borrower's line of business shall be the owning, acquisition, production, refining, transportation and sale of hydrocarbon products;
- (iv) make any investments or lend money to any party without the prior written consent of the Bank except for short-term employee loans not exceeding \$40,000 in the aggregate;
- (v) except for Permitted Distributions, make any payment of interest on or principal of any debt subordinated to the Loan or any dividend payments or distributions to its shareholders without the prior written consent of the Bank;
- (vi) make capital expenditures in any fiscal year of more than \$200,000;
- (vii) make any change in the address of its chief executive office without the prior written consent of the Bank, which consent shall not be unreasonably withheld;
- (viii) sell or assign the accounts, contract rights or receivables pertaining to its business or sell, lease, abandon or otherwise dispose of, directly or indirectly, its assets except in ordinary course of business;

- (ix) allow its Current Ratio to be less than 2.10:1.0;
- (x) allow its Fixed Charge Coverage Ratio to be less than 1.40:1.0 on a quarterly basis; provided, that the Fixed Charge Coverage Ratio shall not be less than 1.55:1.0 in any two (2) consecutive quarters;
- (xi) allow its Fixed Charge Coverage Ratio to be less than 1.65:1.0 on a rolling four-quarter basis; or
- (xii) allow the interest rate on the Borrower's indebtedness to Saudi Fal or Arabian Shield to be greater than the interest rate hereunder at any time.

(d) Distributions. For purposes of Section 9(c) hereof, "Permitted Distribution" shall mean an Administrative Distribution, Interest Distribution, or Excess Distribution, subject to the following conditions:

- (i) An Administrative Distribution shall be a Permitted Distribution only if (1) no Event of Default has occurred and is continuing, or will be caused by such distribution, (2) the

Commitment does not exceed the Borrowing Base, (3) the expenses related to such distribution are properly documented and such documentation is provided to the Bank prior to such distribution, and (4) the aggregate annual amount of such distributions does not exceed USD 60,000.

- (ii) Subject to the additional conditions in Subsection (iv) below, an Interest Distribution shall be a Permitted Distribution provided that such distributions shall not exceed USD 17,500 per month and represents interest actually owed to Saudi Fal and Arabian Shield.
- (iii) Subject to the additional conditions in Subsection (iv) below, an Excess Distribution shall be a Permitted Distribution only if such distribution is applied to the principal of any debt outstanding by the Borrower to Saudi Fal or Arabian Shield.
- (iv) Notwithstanding the provisions of Subsections (ii) and (iii) above, no Excess Distribution or Interest Distribution shall be a Permitted Distribution unless the following conditions are met:
 - (1) the aggregate of all such distributions in any fiscal quarter may not exceed 25% of Borrower's net

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income from the immediately preceding fiscal quarters;

- (2) the aggregate of such distributions for any four quarter period may not exceed 25% of Borrower's income for the four quarter period ending with the quarter immediately preceding the quarter in which the distribution is made;
- (3) the Borrower's Current Ratio for the quarter immediately preceding such distribution is not less than 2.25:1.0;
- (4) the Borrower's Fixed Charge Coverage Ratio for the quarter immediately preceding such distribution is not less than 1.55:1.0;
- (5) the Borrower's Fixed Charge Coverage Ratio for the immediately preceding four quarters is not less than 1.80:1.0; and
- (6) no Event of Default has occurred and is continuing or will be caused by such distribution.

10. CHANGES IN CIRCUMSTANCES

(a) In the event that any applicable law or regulation shall subject the Bank to any Taxes or impose any reserve deposit or other requirements against any assets or liabilities of the Bank, the result of which is to increase the cost to the Bank of making or maintaining the Credit Facility or to reduce the amount of principal or interest received by the Bank, then the Borrower shall be required to compensate the Bank for such additional cost or reduction.

(b) In the event that any applicable law or regulation shall make it unlawful for the Bank to make or maintain the Credit Facility, then the Bank's obligations hereunder shall terminate, and all amounts owing by the Borrower to the Bank shall become due and repayable forthwith.

(c) If the circumstances contemplated by subclause (a) or (b) above should occur and the Bank intends to invoke the conditions contained therein, then the Bank shall promptly advise the Borrower thereof.

(d) Should the conditions of subsection (a) above be invoked and

the Borrower find the resultant additional cost to be unaccept-

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able, then the Borrower shall prepay any amounts outstanding hereunder on the next Payment Date.

(e) If the Borrower prepays any amounts outstanding hereunder in accordance with subsection (d) above, then it shall nonetheless compensate the Bank for additional costs defined under subsection (a) above up to and including the date of prepayment.

11. FEES, COSTS AND EXPENSES

(a) The Borrower shall pay to the Bank upon demand, all reasonable costs, charges and expenses (including legal fees) incurred by the Bank in connection with the preparation, execution, amendment and enforcement of this Restated Agreement and the Security Documents and the preservation of the Bank's rights hereunder and thereunder.

(b) The Borrower shall pay to the Bank within ninety (90) of the Closing Date a facility fee of USD 25,000.

(c) The Borrower shall pay a commitment fee to the Bank on the unused portion of the Credit Facility at the rate of 1/2 of 1% per annum on such unused portion, payable quarterly in arrears on the last day of each such quarter and commencing September 30, 1996.

(d) The obligations of the Borrower under this Section 12 shall survive the repayment of all amounts outstanding hereunder and all interest due thereon.

12. PAYMENTS

(a) All payments hereunder shall be made to the following account:

Unibank New York
For the account of Den norske Bank, New York Branch
Account No. 28764999
Ref. South Hampton Refining Company

(b) In the event of any payments hereunder not being received on the due date therefor, interest will be charged by the Bank from the due date until the date that payment is received at a rate corresponding to the aggregate of the Margin plus 2% (two percent) and the Prime Rate as defined in Section 5(a)(i) hereof. Subject to the provisions of Section 5(c) hereof, interest charged under this subsection (b) shall be added to the defaulted amount on each Payment Date until the defaulted amount is repaid in full.

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(c) All payments to be made by the Borrower hereunder shall be made without set-off or counterclaim and free and clear or and without deduction for or on account of any present or future Taxes of any nature now or hereafter imposed unless the Borrower is compelled by law to make payment subject to any such Tax. In that event the Borrower shall pay to the Bank such additional amounts as may be necessary to insure that the Bank receives a net amount which the Bank would have received had payment not been made subject to such Tax.

(d) If the Credit Facility or any part thereof is, for any reason whatsoever, prepaid or repaid on a day other than a Payment Date, the Borrower shall pay to the Bank on request such amount or amounts as may be necessary to compensate the Bank for any loss or premium or penalty incurred by it in respect of the liquidation or reemployment of funds borrowed for the purpose of maintaining such Facility.

13. CALCULATION

All interest, commission and any other payments hereunder of an annual nature shall accrue from day to day and be calculated on the actual number of days elapsed and on the basis of a 365 or 366 day year, as appropriate.

14. EVENTS OF DEFAULT

Upon notice from the Bank to the Borrower, the obligations of the Bank hereunder shall terminate forthwith and any amounts outstanding under this Restated Agreement and the Note (including interest accrued thereon) shall become immediately repayable (together with any compensatory amounts necessary) if any of the following events of default ("Events of Default") has occurred under this Restated Agreement:

(a) If the Borrower fails to pay any sum due hereunder on the due date.

(b) If the Borrower defaults in the due performance and observance of any of the terms, covenants, undertakings and conditions on its part contained herein or in the Security Documents and such default continues unremedied for a period of 10 days.

(c) If any representation made by the Borrower in this Restated Agreement or any notice, certificate, or statement delivered or made pursuant hereto or under the Security Documents proves to be incorrect, inaccurate or misleading in any material manner when made.

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(d) If a default is declared under any of the Security Documents.

(e) If a distress or other execution is levied upon, or against any substantial part of the property of the Borrower and is not discharged within 15 days.

(f) If the Borrower is unable to or admits in writing its inability to pay their debts as they mature, or makes a general assignment for the benefit of its creditors.

(g) If any proceedings are commenced in, or any order or judgment is given by, any competent court for the liquidation, winding up or reorganization of the Borrower or any order shall be made by any competent court or resolution passed by the Borrower for the appointment of a receiver or a similar functionary for all or a substantial part of its assets, save for the purpose of amalgamation, reorganization or merger not involving insolvency the terms of which shall have received the prior written approval of the Bank, and as otherwise permitted herein.

(h) If the Borrower ceases or threatens to cease to carry on its business or disposes or threatens to dispose of a substantial part of its business, properties, or assets or the same are seized or appropriated for any reason and not released within 30 days.

(i) If any license, consent, permission or approval required in connection with this Restated Agreement or any Security Document is revoked, terminated or modified in a manner which would materially restrict or limit the operation of any property owned or operated by the Borrower.

(j) Default by the Borrower under any other agreement or indenture for the borrowing of money or the guarantee of a third party's obligations.

(k) If Nicholas N. Carter shall cease to be President of the Borrower.

Provided, however, that notwithstanding anything to the contrary in this Restated Agreement, in the event the Borrower has cured any Event of Default prior to the Bank having given notice of acceleration of the amounts owed under this Restated Agreement with respect to such Event of Default, then such Event of Default shall be deemed not to have occurred and the Bank shall

not be entitled to accelerate the Borrower's payment obligations hereunder.

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15. NOTICES AND CORRESPONDENCE

(a) Except as otherwise provided in this Section 16, all notices, requests, consents, demands and other communications provided for or permitted hereunder shall be effective when duly deposited in the mails, certified, return receipt requested, or delivered to Federal Express or similar courier company or transmitted by telex or telefax, addressed to the respective party at the address set forth below, except that notices to the Bank shall not be effective until received.

Bank: Den norske Bank ASA, Representative Office
333 Clay Street, Suite 4890
Houston, Texas 77002
Telefax No. (713) 757-1167
Attention: Byron Cooley

with a copy to

Den norske Bank ASA, New York Branch
200 Park Avenue, 31st Floor
New York, New York 10166-0396
Telefax No. (212) 681-4123
Attention: Customer Service

Borrower: South Hampton Refining Company
Highway 418
Silsbee, Texas 77656
Telefax No.: (409) 385-2453
Attention: President

(b) Either of the parties hereto may change its respective address by notice in writing given to the other party to this Restated Agreement.

(c) All information required to be provided by the Borrower to the Bank pursuant to Section 9(b) above shall be sent to the Bank at the above Houston address by first class U.S. mail and to the Oslo address by first class air mail.

(d) Time is of the essence of this Restated Agreement but no failure or delay on the part of the Bank to exercise any power or right under this Restated Agreement shall operate as a waiver thereof or preclude the exercise of any other power or right. The remedies provided herein are cumulative, and are not exclusive of any remedies provided by law.

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16. GOVERNING LAW AND JURISDICTION

THIS AGREEMENT SHALL BE GOVERNED BY, AND CONSTRUED IN ACCORDANCE WITH, THE LAWS OF THE STATE OF NEW YORK AND THE BORROWER HEREBY IRREVOCABLE SUBMITS TO THE JURISDICTION OF THE COURTS OF THE STATE OF NEW YORK AND THE FEDERAL COURTS LOCATED IN NEW YORK.

17. FINAL AGREEMENT

THIS WRITTEN LOAN AGREEMENT REPRESENTS THE FINAL AGREEMENT BETWEEN THE PARTIES, COMPLETELY REPLACES CREDIT AGREEMENT REFERRED TO HEREIN, AND MAY NOT BE CONTRADICTED BY EVIDENCE OF PRIOR, CONTEMPORANEOUS OR SUBSEQUENT ORAL AGREEMENTS OF THE PARTIES. THERE ARE NO UNWRITTEN AGREEMENTS BETWEEN THE PARTIES.

18. COUNTERPARTS

The Agreement shall be executed in any number of counterparts each of which, when so executed, shall be deemed an original, but all such counterparts shall constitute but one and the same instrument.

IN WITNESS whereof the parties hereto have caused this Agreement to be duly executed by their duly authorized representatives.

SOUTH HAMPTON REFINING COMPANY

By: _____
Name: _____
Title: _____

DEN NORSKE BANK ASA

By: _____
Name: _____
Title: _____

By: _____
Name: _____
Title: _____

SOUTH HAMPTON REFINING COMPANY

PROMISSORY NOTE

October 15, 1996

USD 1,965,000.00

FOR VALUE RECEIVED, SOUTH HAMPTON REFINING COMPANY (herein called the "Undersigned") hereby promises to pay to Den norske Bank ASA, or order, on or before December 31, 1998 on demand, ONE MILLION NINE HUNDRED SIXTY-FIVE THOUSAND AND NO/100 DOLLARS OF THE UNITED STATES OF AMERICA (USD 1,965,000.00) and to pay interest on the unpaid portion of said principal sum outstanding from time to time, as hereinafter provided.

Principal and Interest

1.1 (a) Interest on this Note shall be payable at the times and the rates as provided in Section 5 of the Amended and Restated Credit Agreement (the "Restated Credit Agreement") dated October 15, 1996, between the Undersigned and the payee hereof.

(b) In case any payment of principal or interest is not paid when due, additional interest at the rate determined as provided in Section 13(b) of the Restated Credit Agreement shall be payable on all overdue principal and, to the extent that the same may be lawful, on all overdue interest. 1.2 Interest shall be calculated on the outstanding principal amounts and on the basis of the actual number of days and a year of 365 or 366 days, as appropriate.

1.3 The principal of this Note shall be payable as provided in Section 6 of the Restated Credit Agreement.

3. Inventory (at market price)*	
Raw materials	USD _____
Finished products	USD _____
60%	USD _____
5. Total 1, 2 and 3	USD _____
6. Outstanding to DnB	USD _____

Certified as true and correct:

SOUTH HAMPTON REFINING COMPANY

By: _____
Title: _____

Date: _____ 199____
_____, ____

* Detailed listing attached

RATIFICATION OF SECURITY AGREEMENT

This Ratification of Security Agreement ("Ratification") is made and entered into as of the ____ day of _____, 1996 by and between South Hampton Refining Company, a Delaware corporation ("Borrower") and DEN NORSKE BANK ASA, a Norwegian bank ("Bank" or "Secured Party"). For and in consideration of the mutual covenants and agreements herein contained, Borrower and Secured Party hereby ratify as of the date of this Ratification that certain Security Agreement (the "Security Agreement") between Borrower and Secured Party dated as of the 14th day of January, 1985, relating to the loan by the Bank to the Borrower as more fully described herein.

WHEREAS, Borrower and Bank entered into that certain Credit Agreement dated March 3, 1988 (as amended from time to time, the "1988 Credit Agreement");

WHEREAS, Borrower and Bank executed the Amended and Restated Credit Agreement of even date herewith (the "Restated Credit Agreement"), amending and restating the 1988 Credit Agreement, to, among other things, provide for a revolving loan facility in an aggregate principal amount not to exceed ONE MILLION NINE HUNDRED SIXTY-FIVE THOUSAND AND NO/100 DOLLARS (\$1,965,000.00) (the "Loan") and Secured Party has required execution of this Ratification to confirm the continued application of the Security Agreement to the Loan made pursuant to the Restated Credit Agreement.

NOW THEREFORE, Borrower and Secured Party agree as follows:

The Security Agreement shall remain unchanged and the terms, conditions, representations, warranties, and covenants of said Security Agreement are true as of the date hereof, are ratified and confirmed in all respects and shall be continuing and binding upon Borrower and shall be fully applicable to all loans made pursuant to the Restated Credit Agreement, including, without limitation, the Loan.

This Ratification shall be deemed to be a contract under and subject to, and shall be construed for all purposes in accordance with the laws of the State of Texas.

IN WITNESS WHEREOF, the parties have caused this Ratification to be executed by their duly authorized officers as of the ____ day of _____, 1996.

SOUTH HAMPTON REFINING COMPANY

By: _____
Name:
Title: President

DEN NORSKE BANK ASA

By: _____
Name: _____
Title: _____

By: _____
Name: _____
Title: _____

RATIFICATION OF PLEDGE AGREEMENT

This Ratification of Pledge Agreement ("Ratification") is made and entered into as of the ____ day of _____, 1996 by and between American Shield Refining Company, a Delaware corporation ("Pledgor") and DEN NORSKE BANK ASA, a Norwegian bank ("Bank" or "Pledgee"). For and in consideration of the mutual covenants and agreements herein contained, Pledgor and Pledgee hereby ratify as of the date of this Ratification that certain Pledge Agreement and Irrevocable Proxy ("Pledge") between Pledgor and Pledgee dated as of the 13th day of December, 1990, relating to the loan in an amount of up to \$1,965,000.00 to South Hampton Refining Company, a Texas corporation ("Borrower").

WHEREAS, Borrower and Bank entered into that certain Credit Agreement dated March 3, 1988 (as amended from time to time, the "1988 Credit Agreement");

WHEREAS, Borrower and Bank executed the Amended and Restated Credit Agreement of even date herewith (the "Restated Credit Agreement"), amending and restating the 1988 Credit Agreement, to, among other things, provide for a revolving loan facility in an aggregate principal amount not to exceed ONE MILLION NINE HUNDRED SIXTY-FIVE THOUSAND AND NO/100 DOLLARS (\$1,965,000.00) (the "Loan") and Pledgee has required execution of this Ratification to confirm the continued application of the Pledge Agreement to the Loan made pursuant to the Restated Credit Agreement.

NOW THEREFORE, Pledgor and Pledgee agree as follows:

The Pledge Agreement shall remain unchanged and the terms, conditions, representations, warranties, and covenants of said Pledge Agreement are true as of the date hereof, are ratified and confirmed

in all respects and shall be continuing and binding upon Pledgor and shall be fully applicable to all loans made pursuant to the Restated Credit Agreement, including, without limitation, the Loan.

This Ratification shall be deemed to be a contract under and subject to, and shall be construed for all purposes in accordance with the laws of the State of Texas.

IN WITNESS WHEREOF, the parties have caused this Ratification to be executed by their duly authorized officers as of the ____ day of _____, 1996.

AMERICAN SHIELD REFINING COMPANY

By: _____
Name:
Title: President

DEN NORSKE BANK ASA

By: _____
Name: _____
Title: _____

By: _____
Name: _____
Title: _____

RATIFICATION OF ASSIGNMENT OF INSURANCES

This Ratification of Assignment of Insurances ("Ratification") is made and entered into as of the ____ day of _____, 1996 by and among South Hampton Refining Company, a Delaware corporation ("Borrower"), Gulf State Pipe Line Company, Inc. ("Gulf State") and DEN NORSKE BANK ASA, a Norwegian bank ("Bank" or "Assignee"). For and in consideration of the mutual covenants and agreements herein contained, Borrower, Gulf State and Assignee hereby ratify as of the date of this Ratification that certain Assignment of Insurances (the "Assignment") among Borrower, Gulf State and Assignee dated as of the 3rd day of March, 1988, relating to the loan by the Bank to the Borrower as more fully described herein.

WHEREAS, Borrower and Bank entered into that certain Credit Agreement dated March 3, 1988 (as amended from time to time, the "1988 Credit Agreement");

WHEREAS, Borrower and Bank executed the Amended and Restated Credit Agreement of even date herewith (the "Restated Credit Agreement"), amending and restating the 1988 Credit Agreement, to, among other things, provide for a revolving loan facility in an aggregate principal amount not to exceed ONE MILLION NINE HUNDRED SIXTY-FIVE THOUSAND AND NO/100 DOLLARS (\$1,965,000.00) (the "Loan") and Assignee has required execution of this Ratification to

confirm the continued application of the Security Agreement to the Loan made pursuant to the Restated Credit Agreement.

NOW THEREFORE, Borrower, Gulf State and Assignee agree as follows:

The Assignment shall remain unchanged and the terms, conditions, representations, warranties, and covenants of said Assignment are true as of the date hereof, are ratified and confirmed in all respects and shall be continuing and binding upon Borrower and Gulf State and shall be fully applicable to all loans made pursuant to the Restated Credit Agreement, including, without limitation, the Loan.

This Ratification shall be deemed to be a contract under and subject to, and shall be construed for all purposes in accordance with the laws of the State of Texas.

IN WITNESS WHEREOF, the parties have caused this Ratification to be executed by their duly authorized officers as of the ____ day of _____, 1996.

SOUTH HAMPTON REFINING COMPANY

By: _____
Name:
Title: President

GULF STATE PIPE LINE COMPANY, INC.

By: _____
Name: _____
Title: _____

DEN NORSKE BANK ASA

By: _____
Name: _____
Title: _____

By: _____
Name: _____
Title: _____

SUBORDINATION AGREEMENT

This SUBORDINATION AGREEMENT, dated this 15th day of October, 1996, among Saudi Fal, a limited liability company incorporated under the laws of the Kingdom of Saudi Arabia ("Saudi Fal"), South Hampton Refining Company, a company organized and existing under the laws of the State of Texas (the "Borrower"), Texas Oil & Chemical Co. II, Inc., a company organized and existing under the laws of the State of Texas ("TOCCO"), Arabian Shield Development Company ("ASDC"), a company organized and existing under laws of the State of Delaware, American Shield Refining Company ("ASRC"), a company organized and existing under the laws of the State of Delaware, Gulf State Pipeline Company ("Gulf State"), a company organized and existing under the laws of the State of Texas and Den Norske Bank, ASA, a Norwegian bank ("DnB").

RECITALS

A. Saudi Fal is the owner and holder of certain indebtedness executed by the Borrower and payable to Saudi Fal as more further evidenced by a Second Lien Promissory Note dated the 15th day of October, 1996, attached hereto as Exhibit A and made a part hereof for all purposes (the "Saudi Fal Note");

B. TOCCO is the owner of all of the issued and outstanding common stock of Borrower;

C. Pursuant to the Amended and Restated Credit Agreement for an amount up to \$1,965,000 executed by and between DnB and Borrower (the "Restated Credit Agreement"), DnB has agreed to refinance, renew, extend and restructure its existing loan to Borrower;

D. In order to induce DnB to enter into the Restated Credit Agreement, Saudi Fal, Borrower, TOCCO, ASDC, ASRC and Gulf State have agreed to enter into this Subordination Agreement;

E. Pursuant to 3.2k of the Restated Credit Agreement, DnB has provided that as a condition precedent to the execution of the Amended Credit Agreement and the extension restructuring of its existing loan to Borrower that Saudi Fal, Borrower, TOCCO, ASDC, ASRC and Gulf State execute this Subordination Agreement;

F. Saudi Fal shall subordinate all amounts owed by Borrower or TOCCO to all amounts due to DnB under the Restated Credit Agreement, and Saudi Fal acknowledges and agrees that payments under the Saudi Fal Note shall be limited to the Permitted Distributions as defined in Section 9(d) of the Restated Credit Agreement;

G. Saudi Fal further agrees that notwithstanding the terms of the Saudi Fal Note, the Saudi Fal Note shall not be considered in default even if payments principal or interest

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are not made as required under the Saudi Fal Note if limited by the Permitted Distributions as set forth in the Restated Credit Agreement; and

H. Saudi Fal acknowledges that it is to its benefit for Bank refinance, renew, extend and restructure the DnB Loan to Borrower.

NOW, THEREFORE, in consideration of the DnB refinancing, renewing, extending and restructuring the DnB Loan to Borrower and in further consideration of the recitals set forth above which are made a part of this Subordination Agreement as if fully set forth below, the parties hereto agree as follows:

1. Subordination. (a) Saudi Fal agrees that no payments of principal or interest shall be made to Saudi Fal under the Saudi Fal Note or by Borrower or TOCCO to Saudi Fal under any separate indebtedness unless all payments of any amounts including principal and interest that are due under the Restated Credit Agreement have been paid by Borrower to DnB. Saudi Fal subordinates all amounts owed by it by the Borrower or TOCCO to all amounts outstanding under the Restated Credit Agreement. As stated above, Saudi Fal agrees that notwithstanding the terms of the Saudi Fal Note, the Saudi Fal Note shall not be in default even if payments of principal or interest are not paid as required under Saudi Fal Note if limited by the Permitted Distributions set forth in the Restated Credit Agreement.

2. Representations and Warranties. Saudi Fal and TOCCO hereby represents and warrants as follows:

(a) That each is a corporation duly organized, validly existing and in good standing under the laws of the state, nation or kingdom of its incorporation and are authorized to do business in the jurisdictions in which its ownership of property or

conduct of business legally requires such authorization, and each has full power, authority and legal right to own its properties and assets and to conduct its business as presently conducted or proposed to be conducted.

- (b) It has full power, authority and legal right to execute deliver, and to perform and observe the provisions of this Agreement.
 - (c) The execution, delivery and performance by each of this Agreement has been duly authorized by all necessary corporate or company action. This Agreement constitutes the legal, valid and binding obligation of each, and is enforceable against each in accordance with its terms.
3. Negative Covenants. So long as any part of the DnB Loan shall remain unpaid:
- (a) Saudi Fal will subordinate any security interest, pledge, deed of trust, indenture or assignment that it may have as to any assets of Borrower to the security interests of DnB identified in the Restated Credit Agreement.

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- (b) TOCCO will not sell or otherwise dispose of, or grant any option with respect to or pledge or create or permit to exist any lien, security interest, or other charge or encumbrance upon or with respect to any of the shares of capital stock of Borrower owned by TOCCO except for the creation of the pledge of capital stock that may be required by or as evidenced in the Restated Credit Agreement in favor of DnB.
- (c) No funds from either the Borrower or TOCCO shall be transferred to Saudi Fal or from the Borrower to TOCCO at any time prior to the execution of this Agreement or hereafter in violation of the terms of the Restated Credit Agreement.
- (d) No funds of the Borrower will be transferred to Saudi Fal or to TOCCO other than to pay ordinary and necessary administrative expenses directly related to the operation of the Borrower's refinery in Silsbee, Hardin County, Texas.

4. Consent by DnB to Subordinated Security Interest. DnB consents to lending by Saudi Fal to Borrower of funds up to the face amount of the Saudi Fal Note. DnB also consents to the execution of the Saudi Fal Note. Although no financing statements, security agreements or deed of trusts covering the physical assets of Borrower and Gulf State has yet been executed or recorded, DnB consents to the execution and recording of such financing statements, security agreements or deed of trusts to secure the Saudi Fal Note, provided, however, that any such financing statements, security agreements and deeds of trust executed to cover any such physical assets shall be subordinate to the liens securing the indebtedness of Borrower to DnB which is subject to the Restated Credit Agreement, and that no foreclosure proceedings shall be instituted by the holder of the Saudi Fal Note against any part of the physical assets of Borrower or Gulf State so long as the indebtedness to DnB is outstanding, without the prior written consent of DnB. The limitation herein against foreclosure proceedings without the consent of DnB shall not limit any right the holder of the Saudi Fal Note may have under the terms of the Saudi Fal Note an applicable law to seek a judgment on the Saudi Fal Note and, in accordance with law, to abstract and enforce the collection of any judgment obtained on the Saudi Fal Note, except, that, prior to five (5) years after the date of final maturity of the Saudi Fal Note, no writ of execution or garnishment or other judgment collection process shall be directed against any property, real or personal, against or in which DnB has a lien or security interest. DnB agrees that if it commences a judicial or non-judicial proceeding to enforce its security interest, Saudi Fal shall have the right to either join such an action or commence its own action to protect its right.

5. Restated Credit Agreement. Saudi Fal and TOCCO acknowledge

receipt of a copy of the Restated Credit Agreement, in execution form and hereby consent and agree to the terms and conditions of the Restated Credit Agreement.

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6. Amendments of Agreement. No amendment or waiver of this Agreement nor consent to any departure by Saudi Fal or TOCCO here from shall in any event be effective unless the same are written amendments signed by the duly authorized representative DnB, and then such waiver or consent shall be effective only as to the specific incidence or the specific purpose for which a written amendment has been given.

7. Addresses for Notices. All notices and other communications provided for hereunder shall be in writing (including telegraphic or telefacsimile communication), and if to the parties as set forth below:

Den Norske	TOCCO	Saudi Fal
333 Clay Street	P.O. Box 1636	Fal Holdings Arabia Co., Ltd.
Suite 4890	Silsbee, TX 77656	Al Aruba Road
Houston, TX 77002		P.O. Box 4900
		Riyadh, 11412 Saudi Arabia

or as to any of the above-named parties at such other address as may be designated by such party in a written notice to the all other parties to this Agreement. All such notices and other communications shall, when mailed, telexed or telefacsimiled, be effective, when deposited in the mails or sent by telex or telefacsimile, addressed as herein stated.

8. Governing Law. This Agreement shall be governed by, and construed in accordance with, the laws of the State of Texas.

EXECUTED BY EACH OF THE PARTIES TO THIS AGREEMENT AS NAMED ABOVE ON SEPARATE ORIGINAL SIGNATURE PAGES WHICH THE PARTIES AGREE SHALL BE AFFIXED TO AND DEEMED TO BE AN ORIGINAL OF THIS MODIFICATION AGREEMENT.

SOUTH HAMPTON REFINING COMPANY

By: _____
Its: _____

STATE OF TEXAS
COUNTY OF HARDIN

This instrument was acknowledged before me on the _____ day of _____, 1996, by _____.

Notary Public, State of Texas

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EXECUTION PAGE TO
SUBORDINATION AGREEMENT

ARABIAN SHIELD DEVELOPMENT COMPANY

By:

Its:

STATE OF TEXAS
COUNTY OF DALLAS

This instrument was acknowledged before me on the _____ day of _____,
1996, by _____.

Notary Public, State of Texas

5
EXECUTION PAGE TO
SUBORDINATION AGREEMENT

AMERICAN SHIELD REFINING COMPANY

By:

Its:

STATE OF TEXAS
COUNTY OF DALLAS

This instrument was acknowledged before me on the _____ day of _____,
1996, by _____.

Notary Public, State of Texas

6
EXECUTION PAGE TO
SUBORDINATION AGREEMENT

TEXAS OIL & CHEMICAL CO. II, INC.

By:

Its:

STATE OF TEXAS
COUNTY OF HARDIN

This instrument was acknowledged before me on the _____ day of _____,
1996, by _____.

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EXECUTION PAGE TO
SUBORDINATION AGREEMENT

GULF STATE PIPELINE COMPANY

By: _____
Its: _____

STATE OF TEXAS
COUNTY OF HARDIN

This instrument was acknowledged before me on the _____ day
of _____, 1996, by _____.

Notary Public, State of Texas

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EXECUTION PAGE TO
SUBORDINATION AGREEMENT

SAUDI FAL

By: _____
Its: _____

9
EXECUTION PAGE TO
SUBORDINATION AGREEMENT

DEN NORSKE BANK, ASA

By: _____
Its: _____

STATE OF TEXAS
COUNTY OF _____

This instrument was acknowledged before me on the _____ day of _____, 1996, by _____.

Notary Public, State of Texas

10

TERMINATION AGREEMENT

This Termination Agreement ("Agreement") is made as of _____, 1996, by and among Den norske Bank ASA ("DnB") and Saudi Fal, a Saudi Arabian company ("Saudi Fal").

WHEREAS, DnB and Saudi Fal entered into an Intercreditor Agreement dated _____ (together with any prior agreements, or amendments, modifications or extensions thereof, the "Intercreditor Agreement"); and

WHEREAS, DnB, Saudi Fal and American Shield Refining Company have agreed to the terms of a new intercreditor agreement respecting the relative rights of the parties relating to debts owed them by South Hampton Refining Company (the "New Intercreditor Agreement"); and

WHEREAS, DnB and Saudi Fal desire to terminate their respective rights and obligations under the Intercreditor Agreement.

NOW THEREFORE, for and in consideration of the mutual promises set forth herein, the receipt and legal sufficiency of which is hereby acknowledged, the parties agree as follows:

1. By their execution of this Agreement, the parties hereto agree to terminate the Intercreditor Agreement, and the Intercreditor Agreement, and all rights and obligations thereunder, are hereby terminated. Upon execution of this Agreement by both parties, DnB shall execute and deliver to Saudi Fal, and Saudi Fal shall execute and deliver to DnB, the New Intercreditor Agreement.

2. The parties hereby release each other from all claims, causes of action, debts, liabilities and obligations with respect to the Intercreditor Agreement and the relationship created thereunder except as specifically otherwise provided by this Agreement; it being understood that this Agreement constitutes a complete termination of the Intercreditor Agreement and shall in no way be construed as an amendment, modification, extension or novation thereof.

3. Each party shall indemnify and hold harmless the other from any and all obligations, claims, demands or liabilities now existing or hereafter arising out of the acts or omissions of that party, its agents and employees with respect to the Intercreditor Agreement.

4. This Agreement constitutes the entire agreement of the parties with respect to the subject matter hereof and except as herein provided there are no other oral or written understandings or agreements between the parties hereto relating to the subject matter hereof.

5. This Agreement shall be binding upon the parties and their respective agents, representatives, employees, successors and assigns.

6. This Agreement shall be governed by and construed in accordance with the internal laws of the State of Texas.

IN WITNESS WHEREOF, the parties have duly executed this Termination Agreement as of the date stated above.

SAUDI FAL

By: _____
Name: _____
Title: _____

DEN NORSKE BANK ASA

By: _____
Name: _____
Title: _____

By: _____
Name: _____
Title: _____

RATIFICATION OF SUBORDINATION AGREEMENT

This Ratification of Subordination Agreement (the "Ratification") dated this 15th day of October, 1996, is executed by and among Arabian Shield Development Company ("ASDC"), a company organized and existing under laws of the State of Delaware, American Shield Refining Company ("ASRC"), a company organized and existing under the laws of the State of Delaware, South Hampton Refining Company, a company organized and existing under the laws of the State of Texas (the "Borrower"), Texas Oil & Chemical Co. II, Inc., a company organized and existing under the laws of the State of Texas ("TOCCO"), Gulf State Pipeline Company ("Gulf State"), a company organized and existing under the laws of the State of Texas and Den Norske Bank, ASA, a Norwegian bank ("DnB").

RECITALS

A. DnB has agreed to refinance, renew, extend and restructure a loan of \$1,965,000 to Borrower as evidenced by that certain Amended and Restated Credit Agreement executed by DnB and Borrower dated the 15th day of October, 1996 (the "Restated Credit Agreement").

B. DnB has agreed to refinance, renew, extend and restructure the DnB Loan in consideration for the ratification by ASDC, ASRC, Borrower, TOCCO and Gulf State of their obligations and agreements as set forth in that certain Subordination Agreement dated among the parties hereto as of July 28, 1989, and attached hereto as Exhibit A and made a part hereof for all purposes (the "Subordination Agreement").

C. DnB has further agreed to refinance, renew, extend and restructure the DnB Loan and has acknowledged the indebtedness of Borrower to ASRC as more fully set forth in that certain renewal, extension and modification agreement between Borrower and ASRC dated the 15th day of October, 1996 (the "ASRC Modification Agreement").

D. DnB has further agreed to refinance, renew, extend and restructure the DnB Loan and has acknowledged the execution by Borrower of a certain indebtedness to Saudi Fal, a limited liability company organized and existing under the laws of the Kingdom of Saudi Arabia ("Saudi Fal") in the amount of \$1,945,773.49 as evidenced by that certain Second Lien Promissory Note executed

by Borrower to Saudi Fal dated the 15th day of October, 1996, and secured by a Subordinated Lien on assets of Borrower.

NOW, THEREFORE, in consideration of DnB refinancing, renewing extending and restructuring the DnB Loan to Borrower and in further consideration of the recital set forth above which are made a part of this Ratification of Subordination Agreement as if fully set forth below, the parties hereto agree as follows:

1. Ratification of Subordination Agreement. ASDC, ASRC, Borrower, TOCCO and Gulf State hereby ratify and confirm the terms and conditions of the Subordination

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Agreement while acknowledging the indebtedness of Borrower to ASRC is now evidenced by a Third Lien Promissory Note dated the 15th day of October, 1996.

2. Saudi Fal Indebtedness. ASDC, ASRC, Borrower, TOCCO and Gulf State hereby acknowledge the indebtedness of Borrower to Saudi Fal as now evidenced by a certain Second Lien Promissory Note dated the 15th day of October, 1996, secured by the assets of the Corporation, but subordinated to the security interest of DnB.

3. Limitation Permitted Distribution. ASDC, ASRC, Borrower, TOCCO and Gulf State acknowledge and agree that payments under the ASRC Note shall be limited to the Permitted Distributions as specified in Section 9(d) of the Restated Credit Agreement. ASRC agrees that notwithstanding the terms of the ASRC Note, the ASRC Note will not be in default even if payments of principal or interest are not made under the ASRC Note as limited by the Permitted Distributions set forth in the Restated Credit Agreement.

4. Amendment. No amendment of this Ratification or of the Subordination Agreement shall be effective except and until executed in writing by all the parties hereto and such amendment shall become effective only in the specific instance for any specific purpose that such may be given.

5. Counterparts. This Modification Agreement shall be executed in multiple counterparts, all of which shall be considered a single document. Each of the parties to this Agreement named above shall execute this Modification Agreement on separate original signature pages, which parties agree shall be affixed to and deemed to be an original.

Executed by the parties hereto and delivered as of the date first above written.

SOUTH HAMPTON REFINING COMPANY

By: _____
Its: _____

STATE OF TEXAS
COUNTY OF HARDIN

This instrument was acknowledged before me on the _____ day of _____, 1996, by _____.

Notary Public, State of Texas

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EXECUTION PAGE TO
RATIFICATION OF SUBORDINATION AGREEMENT

ARABIAN SHIELD DEVELOPMENT COMPANY

By: _____
Its: _____

STATE OF TEXAS
COUNTY OF DALLAS

This instrument was acknowledged before me on the _____ day of _____,
1996, by _____.

Notary Public, State of Texas

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EXECUTION PAGE TO
RATIFICATION OF SUBORDINATION AGREEMENT

AMERICAN SHIELD REFINING COMPANY

By: _____
Its: _____

STATE OF TEXAS
COUNTY OF DALLAS

This instrument was acknowledged before me on the _____ day of _____,
1996, by _____.

Notary Public, State of Texas

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EXECUTION PAGE TO
RATIFICATION OF SUBORDINATION AGREEMENT

TEXAS OIL & CHEMICAL CO. II, INC.

By: _____
Its: _____

STATE OF TEXAS
COUNTY OF HARDIN

This instrument was acknowledged before me on the _____ day of _____,
1996, by _____.

Notary Public, State of Texas

5
EXECUTION PAGE TO
RATIFICATION OF SUBORDINATION AGREEMENT

GULF STATE PIPELINE COMPANY

By: _____
Its: _____

STATE OF TEXAS
COUNTY OF HARDIN

This instrument was acknowledged before me on the _____ day of _____,
1996, by _____.

Notary Public, State of Texas

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EXECUTION PAGE TO
RATIFICATION OF SUBORDINATION AGREEMENT

DEN NORSKE BANK, ASA

By: _____
Its: _____

STATE OF TEXAS
COUNTY OF _____

This instrument was acknowledged before me on the _____ day of _____,
1996, by _____.

Notary Public, State of Texas

SOUTH HAMPTON REFINING COMPANY
CERTIFICATE OF SECRETARY

I, _____, Secretary of South Hampton Refining Company (the "Borrower") do hereby certify as follows:

- 1) At the meeting of the Board of Directors of the Borrower duly and legally called and held on the _____ day of _____, 19_____ at which meeting in quorum with the President voting throughout, the Resolutions attached hereto as Exhibit A were duly adopted, and such Resolutions are now in full force and effect and have not been amended, modified, or revoked.
- 2) Attached hereto as Exhibit B is a true, correct and complete copy of the Bylaws of Borrower as in effect at all times since the date of the Resolution set forth in Exhibit A attached hereto and from and after such date to the dates hereof.

IN WITNESS HEREOF, I have set my hand this ____ day of _____1996.

SECRETARY

I, _____, President of Borrower do hereby certify that _____ is the duly elected and qualified Secretary of the Borrower and that the signature above is his genuine signature.

IN WITNESS HEREOF, I have set my hand this ____ day of _____, 1996.

PRESIDENT

SOUTH HAMPTON REFINING COMPANY
CERTIFICATE OF SECRETARY

I, Scott Young, Secretary of South Hampton Refining Company (the "Borrower"), do hereby certify as follows:

1. Attached hereto as Exhibit \$ is a true, correct and complete copy of the Bylaws of the Borrower as in effect at all times since June 9, 1987 to and including the date hereof.

2. At a meeting of the Board of Directors of the Borrower, duly and legally called and held on the 29th day of February, 1988, at which meeting a quorum was present and voting throughout, the Resolutions attached hereto as Exhibit A were duly adopted, and such Resolutions are now in full force and effect and have not been amended, modified or revoked.

IN WITNESS WHEREOF. I have hereunto set my hand this day of February, 1988.

Scott Young, Secretary

I, the under signed President of the Company , do hereby certify that Scott Young is the duly elected and qualified Secretary of the Company and that the signature above is his genuine signature.

IN WITNESS WHEREOF, I have hereunto set my hand this day of March, 1988.

Nicholas Carter

1
EXHIBIT A

WHEREAS, the Board of Directors deems it advisable and in the best interest of the Corporation to enter into a Credit Agreement by and among the Corporation and Den norske Creditbank (the "Bank");

NOW THEREFORE, BE IT RESOLVED, that the Corporation enter into the Credit Agreement with the Bank as lender to loan up to \$5,156,694.43 to Corporation;

RESOLVED, that such borrowing be evidenced by the Promissory Note to be executed by the Corporation as maker, to be delivered pursuant to a Credit Agreement dated as of February 29, 1988, between the Corporation and the Bank (the "Credit Agreement"), and the form of Credit Agreement (and all exhibits thereto) presented to and reviewed by the Board of Directors be and it hereby is, authorized and approved in all respects, and the President, Secretary or any other officer of the Corporation hereby is authorized to execute and deliver the aforesaid Credit Agreement on behalf of the Corporation, with such Changes, additions, amendments and deletions as any such officer shall deem appropriate, the authorization of the same by the Corporation to be conclusively evidenced by such execution and delivery.

RESOLVED, that pursuant to the terms of the Credit Agreement, the President, Secretary or any officer of the Corporation be, and hereby is, authorized and empowered to execute and deliver to the Bank on the Corporation's behalf all of the Security Documents, as such term is defined in the Credit Agreement, with such additions, deletions and modifications to the Security Documents as any such officer shall deem appropriate, the authorization and approval of the same by the Corporation to be conclusively evidenced by such execution and delivery.

RESOLVED, that the President, Secretary or any other officer of the Corporation be, and hereby is, authorized and empowered, in the name and on behalf of the Corporation, to take or cause to be taken now or in the future, all such action, and to sign, execute, verify, acknowledge, certify to, file and deliver all such instruments, financing statements and documents, as shall in

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the judgment of the President, Secretary or any other officer of the Corporation be necessary, desirable or appropriate in order to perform the obligations of the Corporation under the Credit Agreement and the Security Documents, to effect the aforesaid borrowing, and otherwise to effectuate the purposes of the

foregoing resolutions.

RENEWAL, EXTENSION AND MODIFICATION AGREEMENT

This Renewal, Extension and Modification Agreement (the "Modification Agreement") is entered into and effective as of this 15th day of October, 1996, by and between Arabian Shield Development Company ("ASDC"), a company organized and existing under laws of the State of Delaware, American Shield Refining Company ("ASRC"), a company organized and existing under the laws of the State of Delaware, South Hampton Refining Company, a company organized and existing under the laws of the State of Texas (the "South Hampton"), Texas Oil & Chemical Co. II, Inc., a company organized and existing under the laws of the State of Texas ("TOCCO") and Gulf State Pipeline Company ("Gulf State"), a company organized and existing under the laws of the State of Texas.

RECITALS

A. ASDC is the owner of all the issued and outstanding common stock of ASRC.

B. ASRC is the owner of all the issued and outstanding common stock of TOCCO.

C. TOCCO is the owner of all the issued and outstanding common stock of South Hampton.

D. South Hampton is the owner of all the issued and outstanding common stock of Gulf State.

E. South Hampton is a party to an Amended and Restated Credit Agreement dated the 15th day of October, 1996, (the "Restated Credit Agreement") for an amount of up to \$1,965,000 provided to South Hampton by Den Norske Bank, ASA ("DnB").

F. ASRC is the owner and holder of that certain Second Lien Promissory Note dated July 28, 1989, in the original principal sum of \$510,000 (the "ASRC Note").

G. The ASRC Note is a second lien promissory note secured by a second lien, inferior only to the first lien of DnB, covering all physical assets of South Hampton and Gulf State which second lien is evidenced by financing statements, security agreements and deeds of trust covering all of such physical assets of South Hampton and Gulf State, but with all foreclosure rights under such security agreements and deeds of trust being expressly subject to a Subordination Agreement entered into by the parties hereto and DnB dated July 28, 1989 (the "Subordination Agreement") the terms and conditions of which have been ratified by those parties by a Ratification of Subordination Agreement dated as of the 15th day of October, 1996 (the "Ratification").

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H. South Hampton is indebted to Saudi Fal, a limited liability company organized and existing under the laws of the Kingdom of Saudi Arabia ("Saudi Fal") in the amount of \$1,945,773.49 (the "Saudi Fal Indebtedness").

I. The Saudi Fal Indebtedness is to be evidenced by a certain Second Lien Promissory Note dated October 15, 1996, and to be secured by second lien inferior only to the first lien of DnB covering all the physical assets of South Hampton and Gulf State and which will be evidenced by one or more financing statements, security agreements and deeds of trust covering all of such physical assets, but with all foreclosure rights under such security agreements and deeds of trust being made expressly subject to a Subordination Agreement of even date herewith entered into by and among ASDC, ASRC, TOCCO, South Hampton, Gulf State, Saudi Fal and DnB (the "Subordination Agreement").

J. In order to induce DnB to amend its Restated Credit Agreement with South Hampton as more fully set forth in the Amended and Restated Credit Agreement and in order to induce Saudi Fal to renew and extend the Saudi Fal Note to South Hampton, ASRC has agreement to subordinate the repayment of its indebtedness to both the DnB Note and the Saudi Fal Note.

K. The ASRC indebtedness now shall be evidenced by a Third Lien Promissory Note dated the 15th day of October, 1996 (the "ASRC Note").

NOW, THEREFORE, IN CONSIDERATION Of DnB Refinancing, renewing, extending and restructuring the DnB Loan to South Hampton, in consideration of the renewal and extension by Saudi Fal of the Saudi Fal Note to South Hampton and in further consideration of the recitals set forth above which are made a part of this Modification Agreement as if fully set forth below, the parties hereto agree as follows:

1. Renewal and Extension of Loan. ASRC and South Hampton hereby covenant, contract and agree that the time for payment of the ASRC Note is hereby extended to and shall hereafter be renewed and shall be due and payable on or before December 31, 1998.

2. Modification in Loan Amount. ASRC and South Hampton covenant, contract and agree that the outstanding principal balance of the ASRC Loan shall be modified and increased to \$1,694,605.08.

3. Security for ASRC Note. ASRC acknowledges and South Hampton covenant, contract and agree that the ASRC Note will be secured by a third lien, inferior to (i) the first lien of DnB as set forth in the Restated Credit Agreement and (ii) the second lien of Saudi Fal as specified in the Subordination Agreement, covering all physical assets of South Hampton and Gulf State, but with all foreclosure rights under such security agreements and deeds of trust made expressly subject to the Subordination Agreement of even date herewith entered into among ASDC, ASRC, South Hampton, TOCCO, Gulf State and DnB.

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4. Security for ASRC Note. The following security previously shown as a subordinated second lien shall now be given to secure the ASRC Note and shall be a third lien security interest against the assets of South Hampton and said third lien security interest now acknowledge and as set forth in the following:

- a) Deed of trust given by Gulf State for the benefit of ASRC recorded in Volume 740, Page 042 of the official public records of real property of Hardin County, Texas.
- b) Deed of trust given by Gulf State to ASRC recorded in Volume 221, Page 778 of the official public records of real property of Hardin County, Texas.
- c) Deed of trust given by South Hampton to ASRC recorded in Volume 221, Page 791 of the official public records of real property of Hardin County, Texas.
- d) Deed of trust given by Gulf State to ASRC recorded in Volume 167, Page 432 of the official public records of real property of Hardin County, Texas.
- e) Certain security agreement executed by Gulf State to ASRC granting a security interest in goods, inventory, equipment and fixtures as referenced in Exhibit A attached thereto and incorporated in for all purposes.

5. Limitation as to Permitted Distributions. ASRC acknowledges and agrees that payments under the ASRC Note shall be limited to the Permitted Distributions as defined in Section 9(d) of the Restated Credit Agreement. ASRC agrees that notwithstanding the terms of the ASRC Note, the ASRC Note shall not be in default even if payments of principal or interest are not made as required under the ASRC Note if limited by the Permitted Distributions set forth in the Restated Credit Agreement.

6. Acknowledgement of South Hampton. Except as amended as to the maturity date of the ASRC Note and as to the outstanding principal balance of the ASRC Note and subject to the change in the security interest hereby evidenced, South Hampton covenants, contracts and agrees that all the terms and

conditions of the ASRC Note as renewed, extended and rearranged are hereby ratified and confirmed and shall remain in full force and effect. South Hampton acknowledges and agrees that the outstanding liens, security interest and assignments created by the financing statements, security agreements and deeds of trust hereinafter identified and securing the ASRC Note shall hereafter be valid and subsisting third liens, security interest and assignments.

7. Governing Law. The terms and provisions of this Modification Agreement shall be governed by and construed in accordance with the laws of the State of Texas, except to the extent preempted by the federal law.

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8. Counterparts. This Modification Agreement shall be executed in multiple counterparts, all of which shall be considered a single document. Each of the parties to this Agreement named above shall execute this Modification Agreement on separate original signature pages, which parties agree shall be affixed to and deemed to be an original.

SOUTH HAMPTON REFINING COMPANY

By: _____
Its: _____

STATE OF TEXAS
COUNTY OF HARDIN

This instrument was acknowledged before me on the _____ day of _____, 1996, by _____.

Notary Public, State of Texas

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EXECUTION PAGE TO
RENEWAL, EXTENSION AND MODIFICATION AGREEMENT

ARABIAN SHIELD DEVELOPMENT COMPANY

By: _____
Its: _____

STATE OF TEXAS
COUNTY OF DALLAS

This instrument was acknowledged before me on the _____ day of _____, 1996, by _____.

Notary Public, State of Texas

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EXECUTION PAGE TO
RENEWAL, EXTENSION AND MODIFICATION AGREEMENT

AMERICAN SHIELD REFINING COMPANY

By: _____
Its: _____

STATE OF TEXAS
COUNTY OF DALLAS

This instrument was acknowledged before me on the _____ day of _____,
1996, by _____.

Notary Public, State of Texas

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EXECUTION PAGE TO
RENEWAL, EXTENSION AND MODIFICATION AGREEMENT

TEXAS OIL & CHEMICAL CO. II, INC.

By: _____
Its: _____

STATE OF TEXAS
COUNTY OF HARDIN

This instrument was acknowledged before me on the _____ day of _____,
1996, by _____.

Notary Public, State of Texas

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EXECUTION PAGE TO
RENEWAL, EXTENSION AND MODIFICATION AGREEMENT

GULF STATE PIPELINE COMPANY

By: _____
Its: _____

This instrument was acknowledged before me on the _____ day of _____,
1996, by _____.

Notary Public, State of Texas

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SECOND LIEN PROMISSORY NOTE

\$1,945,773.49

Silsbee, Texas

October 15, 1996

FOR VALUE RECEIVED, the undersigned, South Hampton Refining Company, a Texas corporation (the "Maker"), promises and agrees to pay to Saudi Fal, a limited liability company incorporated under the laws of the Kingdom of Saudi Arabia (the "Payee"), the principal sum of \$1,945,773.49 in legal and lawful money of the United States of America payable at its offices of Fal Holdings Arabia Co., Ltd., Al Aruba Road, P.O. Box 4900, Riyadh, 11412 Saudi Arabia or such other place or places as the holder hereof shall from time to time designate in written notice to Maker. In addition to the principal sum referred to above, Maker agrees to pay interest hereon from the date hereof until maturity at a fluctuating rate per annum which shall from day to day be equal to the lesser of (a) the Maximum Rate (as such term is hereinafter defined), or (b) a rate (the "Contract Rate"), calculated on the basis of the actual days elapsed but computed as if each year consisted of 365 days equal to the sum of (i) the rate announced from time to time by Den Norske Bank, ASA, a Norwegian Bank (the "Bank") as its prime lending rate in effect in its New York, New York office, automatically fluxuating upward and downward with and at the time of each such announcement without special notice to Maker or any other persons plus (ii) one percent (1.00%). Notwithstanding the foregoing, interest on this Note shall on no event exceed the Maximum Rate of nonuserious interest allowed by law (as such term is hereinafter defined). If the Contract Rate at any time shall exceed the Maximum Rate, the interest hereon, during the period of time that the Contract Rate exceeds the Maximum Rate, the rate of interest charged under this Note shall be the Maximum Rate.

The term "Maximum Rate" as used herein shall mean at the particular time in question the maximum rate of interest which, under applicable law, may then be charged on this Note. If such maximum rate of interest changes after the date hereof and this Note provides for a fluctuating rate of interest, the Maximum Rate shall be automatically increased or decreased, as the case may be, without notice to Maker from time to time as of the effective date of each change in such maximum rate. If applicable law ceases to provide for such a maximum rate of interest, the Maximum Rate shall be equal to eighteen percent (18.00%) per annum.

Interest only on this Note shall be due and payable in monthly installments with the first of such monthly installments of interest being due and payable on the 25th day of November, 1996, with the like installment being due and payable on the 25th day of each calendar month thereafter, until the 31st day of December, 1998, at which time the entire unpaid balance of this Note, both principal and accrued and unpaid interest, shall be due and payable, if not sooner paid.

This Note may be prepaid, in whole or in part, without notice or penalty. Any such prepayment shall be applied first toward accrued interest, and the balance, if any, toward principal, but interest shall immediately cease upon amounts of principal prepaid.

It is expressly provided that upon default in the punctual payment of this Note or any part thereof, principal or interest, as the same shall become due and payable, and at the option of the holder, the entire indebtedness shall be matured. In the event default is made in the prompt payment of this Note when due or declared due, and the same is placed in the hands of an attorney for collection, or suit is brought on same, or the same is collected through probate, bankruptcy or other judicial proceedings, then the Maker agrees and promises to pay reasonable attorneys' fees, court costs, deposition and investigation charges, and all expenses of collection, payment and liquidation thereof.

If the Maker shall become insolvent (however such insolvency may be evidence) or if a receiver shall be appointed for or take possession of the assets of Maker, or if a writ or order of attachment of garnishment shall be made or issued against the assets of Maker, or if the Maker shall be dissolved, wound up, liquidated or otherwise terminated or become a party to any merger or consolidation without the written consent of the holder of this Note, or if, after the first lien indebtedness to Den Norske Bank, ASA is paid, Note Maker shall sell substantially all or an integral portion of its assets without the written consent of the holder hereof, or if a default occurs under any instrument now or hereafter executed in connection with or as security for this Note, or if Den Norske Bank, ASA should accelerate the maturity of such indebtedness, file suit against Maker or institute any foreclosure proceedings against any of the assets of Maker, thereupon is the option of the holder of this Note, this Note and any and all other indebtedness of Maker to the holder hereof shall become due and payable.

Except as provided herein, each maker and endorser of this Note expressly waives all notices, demands for payment, presentations for payment, notices of intention to accelerate the maturity, protest and notice of protest, as to this Note and as to each, every and all installments hereof, and consents to and waives notice of any and all renewals, extensions and rearrangements hereof and without affecting the liability and obligations of any party which is not expressly released in writing. It is further agreed that the exercise of any right or remedy conferred upon any holder hereof shall be wholly discretionary with such holder, and such exercise of, or failure to exercise, any such right or remedy shall not in any manner affect, impair or diminish the obligations and liabilities of any party liable hereon or herefore, or be deemed a waiver of any such right or remedy.

Notwithstanding any other provisions to the contrary in this Note or elsewhere, upon any event of default by Maker, Payee agrees to give Maker written notice of such event of default prior to the acceleration of this Note or exercise of any other remedies in connection therewith and Maker shall have a period of thirty (30) days after receipt of such written notice in which to cure any monetary default, and sixty (60) days after receipt of such written notice within which to cure any non-monetary default; provided however, that if any non-monetary default cannot reasonably be cured within said sixty (60) day period, Maker shall have a reasonable period of time following receipt of such written notice within which to cure such default if Maker commences within said initial sixty (60) day period action reasonably calculated to cure such default and thereafter proceeds with reasonable diligence to attempt to cure same.

It is the intention of Maker and Payee to conform strictly to applicable usury laws. Accordingly, no provision of this Note or any agreement entered into in connection with or as security for this Note shall permit Payee to charge, receive, take, or reserve interest in excess of lawful amounts. If any excess occurs, Payee shall, at its option, apply such excess as a credit against principal or otherwise refund such excess to Maker and the effective rate of interest shall automatically be reduced to the maximum rate allowed by applicable law (including the laws of the State of New York and the United States of America). This paragraph shall govern over all provisions of this Note and any agreement entered into in connection with this Note.

The Note and any liens created to secure the Note shall be subordinate

to the payment of that certain Promissory Note dated the 15th day of October, 1996, executed by Maker in favor of Den Norske Bank, ASA and being the renewal, extension, modification of indebtedness of Maker to Den Norske Bank, ASA as more fully set forth in that certain Amended and Restated Credit Agreement for an amount up to \$1,965,000 provided by Den Norske Bank ASA to Maker, and this Note is subject and subordinate to the rights of payment and the rights of prior payment in full of all indebtedness of Maker to Bank pursuant to that certain Amended and Restated Credit Agreement executed by Maker to Den Norske Bank, ASA dated the 15th day of October, 1996.

This Note is made under and shall be construed in accordance with and governed by the laws of the State of Texas, and by the laws of the United States of America as applicable.

EXECUTED this 15th day of October, 1996.

SOUTH HAMPTON REFINING COMPANY

By _____
Its _____

3

THIRD LIEN PROMISSORY NOTE

\$1,694,605.08

Silsbee, Texas

October 15, 1996

FOR VALUE RECEIVED, the undersigned, South Hampton Refining Company, a Texas corporation (the "Maker"), promises and agrees to pay to American Shield Refining Company, a Delaware corporation (the "Payee"), the principal sum of \$1,694,605.08 in legal and lawful money of the United States of America payable at its offices of American Shield Refining Company, 10830 N. Central Expressway, Suite 175, Dallas, Texas 75231, or such other place or places as the holder hereof shall from time to time designate in written notice to Maker. In addition to the principal sum referred to above, Maker agrees to pay interest hereon from the date hereof until maturity at a fluctuating rate per annum which shall from day to days be equal to the lesser of (a) the Maximum Rate (as such term is hereinafter defined), or (b) a rate (the "Contract Rate"), calculated on the basis of the actual days elapsed but computed as if each year consisted of 365 days equal to the sum of (i) the rate announced from time to time by Den Norske Bank, ASA, a Norwegian Bank (the "Bank") as its prime lending rate in effect in its New York, New York office, automatically fluxuating upward and downward with and at the time of each such announcement without special notice to Maker or any other persons plus (ii) one percent (1.00%). Notwithstanding the foregoing, interest on this Note shall on no event exceed the Maximum Rate of nonuserious interest allowed by law (as such term is hereinafter defined). If the Contract Rate at any time shall exceed the Maximum Rate, the interest hereon, during the period of time that the Contract Rate exceeds the Maximum Rate, the rate of interest charged under this Note shall be the Maximum Rate.

The term "Maximum Rate" as used herein shall mean at the particular time in question the maximum rate of interest which, under applicable law, may then be charged on this Note. If such maximum rate of interest changes after the date hereof and this Note provides for a fluctuating rate of interest, the Maximum Rate shall be automatically increased or decreased, as the case may be, without notice to Maker from time to time as of the effective date of each change in such maximum rate. If applicable law ceases to provide for such a maximum rate of interest, the Maximum Rate shall be equal to eighteen percent (18.00%) per annum.

Interest only on this Note shall be due and payable in monthly installments with the first of such monthly installments of interest being due and payable on the 25th day of November, 1996, with the like installment being

due and payable on the 25th day of each calendar month thereafter, until the 31st day of December, 1998, at which time the entire unpaid balance of this Note, both principal and accrued and unpaid interest, shall be due and payable, if not sooner paid.

This Note may be prepaid, in whole or in part, without notice or penalty. Any such prepayment shall be applied first toward accrued interest, and the balance, if any, toward principal, but interest shall immediately cease upon amounts of principal prepaid.

It is expressly provided that upon default in the punctual payment of this Note or any part thereof, principal or interest, as the same shall become due and payable, and at the option of the holder, the entire indebtedness shall be matured. In the event default is made in the prompt payment of this Note when due or declared due, and the same is placed in the hands of an attorney for collection, or suit is brought on same, or the same is collected through probate, bankruptcy or other judicial proceedings, then the Maker agrees and promises to pay reasonable attorneys' fees, court costs, deposition and investigation charges, and all expenses of collection, payment and liquidation thereof.

If the Maker shall become insolvent (however such insolvency may be evidence) or if a receiver shall be appointed for or take possession of the assets of Maker, or if a writ or order of attachment of garnishment shall be made or issued against the assets of Maker, or if the Maker shall be dissolved, wound up, liquidated or otherwise terminated or become a party to any merger or consolidation without the written consent of the holder of this Note, or if, after the first lien indebtedness to Den Norske Bank, ASA is paid, Note Maker shall sell substantially all or an integral portion of its assets without the written consent of the holder hereof, or if a default occurs under any instrument now or hereafter executed in connection with or as security for this Note, or if Den Norske Bank, ASA should accelerate the maturity of such indebtedness, file suit against Maker or institute any foreclosure proceedings against any of the assets of Maker, thereupon is the option of the holder of this Note, this Note and any and all other indebtedness of Maker to the holder hereof shall become due and payable.

Except as provided herein, each maker and endorser of this Note expressly waives all notices, demands for payment, presentations for payment, notices of intention to accelerate the maturity, protest and notice of protest, as to this Note and as to each, every and all installments hereof, and consents to and waives notice of any and all renewals, extensions and rearrangements hereof and without affecting the liability and obligations of any party which is not expressly released in writing. It is further agreed that the exercise of any right or remedy conferred upon any holder hereof shall be wholly discretionary with such holder, and such exercise of, or failure to exercise, any such right or remedy shall not in any manner affect, impair or diminish the obligations and liabilities of any party liable hereon or herefore, or be deemed a waiver of any such right or remedy.

Notwithstanding any other provisions to the contrary in this Note or elsewhere, upon any event of default by Maker, Payee agrees to give Maker written notice of such event of default prior to the acceleration of this Note or exercise of any other remedies in connection therewith and Maker shall have a period of thirty (30) days after receipt of such written notice in which to cure any monetary default, and sixty (60) days after receipt of such written notice within which to cure any non-monetary default; provided however, that if any non-monetary default cannot reasonably be cured within said sixty (60) day period, Maker shall have a reasonable period of time following receipt of such written notice within which to cure such default if Maker commences within said initial sixty (60) day period action reasonably calculated to cure such default and thereafter proceeds with reasonable diligence to attempt to cure same.

It is the intention of Maker and Payee to conform strictly to applicable usury laws. Accordingly, no provision of this Note or any agreement entered into in connection with or as security for this Note shall permit Payee to charge, receive, take, or reserve interest in excess of lawful amounts. If any excess occurs, Payee shall, at its option, apply such excess as a credit against principal or otherwise refund such excess to Maker and the effective rate of interest shall automatically be reduced to the maximum rate allowed by applicable law (including the laws of the State of New York and the United States of America).

This paragraph shall govern over all provisions of this Note and any agreement entered into in connection with this Note.

The Note and any liens created to secure the Note shall be subordinate to the payment of that certain Promissory Note dated the 15th day of October, 1996, executed by Maker in favor of Den Norske Bank, ASA and being the renewal, extension, modification of indebtedness of Maker to Den Norske Bank, ASA as more fully set forth in that certain Amended and Restated Credit Agreement for an amount up to \$1,965,000 provided by Den Norske Bank ASA to Maker, and this Note is subject and subordinate to the rights of payment and the rights of prior payment in full of all indebtedness of Maker to Bank pursuant to that certain Amended and Restated Credit Agreement executed by Maker to Den Norske Bank, ASA dated the 15th day of October, 1996.

The Note and any liens created to secure the Note shall be subordinate (i) to the payment of that certain Promissory Note dated the 15th day of October, 1996, executed by Maker in favor of Den Norske Bank, ASA (the "Bank") and being the renewal, extension, modification of indebtedness of Maker to Bank as more fully set forth in that certain Amended and Restated Credit Agreement dated October 15, 1996 for an amount up to \$1,965,000 provided by Bank to Maker; (ii) to the payment of that certain Second Lien Promissory Note of Maker to Saudi Fal, a limited liability company incorporated under the laws of the Kingdom of Saudi Arabia in the amount of \$1,945,773.49 dated October 15, 1996.

This Note is made under and shall be construed in accordance with and governed by the laws of the State of Texas, and by the laws of the United States of America as applicable.

EXECUTED this 15th day of October, 1996.

SOUTH HAMPTON REFINING COMPANY

By _____
Its _____

ARABIAN SHIELD DEVELOPMENT COMPANY

10830 North Central Expressway, Suite 175
Dallas, Texas 75231
(214) 692-7872

November 15, 1996

Sheikh Fahad Al-Athel
P.O. Box 4900
Riyadh 11412
Saudi Arabia

Dear Sheikh Fahad Al-Athel:

Arabian Shield Development Company, a Delaware Corporation, agrees to sell you Four Hundred Fifty Thousand Shares (450,000) of its authorized and unissued common stock, par value \$.10 per share, and you agree to purchase such shares at the price of 1.00 Dollar (one) per share. Payment for these shares shall be made on the following schedule:

\$100,000 to be paid on the date of your signing; and
\$100,000 monthly thereafter.

These shares have not been registered under the United States Securities Act of 1933 (the "Act"), as amended, and are being sold to you in reliance upon one or more exemptions from the registration requirements of the Act, including but not limited to, the exemptions set forth in Regulation S relating to offers and sales made outside the United States of America.

By your execution of this letter agreement, you represent to the Company as follows:

1. You are not a citizen or resident of the United States of America;
2. You are purchasing the shares for your own account for investment and not with a view to the resale or distribution of the shares within, or to citizens or residents of, the United States of America;
3. You are not purchasing the shares for the account or benefit or a citizen or resident of the United States of America or any partnership or corporation organized or incorporated under the laws of any jurisdiction in the United States of America;

Sheikh Fahad Al-Athel
Page 2
November 15, 1996

4. At the time you are executing this letter agreement, you are outside the United States of America;
5. You have received or have had access to all information you consider necessary or advisable in order to enable you to make an informed decision concerning your purchase of the shares; and
6. You have such knowledge and experience in business and financial matters that you are capable of evaluating the merits and risks or investing in the shares, and you are able to bear the economic risk of investing in the shares.

You further agree that the shares may not be offered for sale, sold, or otherwise disposed of within or to United States citizens or residents unless the shares are subsequently registered under the Act or an exemption from

registration is available. The certificate representing the shares will contain a restrictive legend with respect to the foregoing. In the event that by reason of your acquisition of the shares you are required to make any filings pursuant to the United States Securities Exchange Act of 1934, as amended, the certificate representing the shares will not be issued to you until all applicable filing requirements have been satisfied.

Very truly yours,

ARABIAN SHIELD DEVELOPMENT COMPANY

By: /s/ Hatem El-Khalidi

AGREED TO:

By: /s/ Sheikh Fahad Al-Athel

Date: November 30, 1996

FINANCIAL AND LEGAL SERVICES AND ADVICE AGREEMENT

This Agreement is made this day May 20, 1996 by and between:

1. Arabian Shield Development Co., an American Company having its registered office at the State of Delaware and a branch in Jeddah City registered under the No: 4030097805 dated 8/3/1414 H represented in this Agreement by its President, Hatem Hussein El-Khalidi hereinafter referred to as the "First Party".
2. Legal Advisor Nasir Ali Kadasah and Dar Al Khaleej for Researches and Economic Advisors represented by Mr. Tawfiq Abdulaziz Al-Sowailim, hereinafter referred to as the "Second Party".

Whereas the First Party has got a mining lease to exploit Al Masane area located in the Southern Kingdom of Saudi Arabia under the Royal Decree No. M/17 dated 1/12/1413H for a term of Thirty (30) years according to the Mining Lease Agreement attached with the said Royal Decree.

Whereas the First Party desires to participate with "The Saudi Company For Mining Industry" a Saudi limited liability company "under formation" which shall purchase fifty percent (50%) of the First Party's share in the mining lease and to mutually apply to obtain an industrial license and finance the project, and, to apply to the Minister of Petroleum and Mineral Resources to transfer the mining lease to the First Party and the Saudi Company jointly and severally.

And, whereas the Second Party is able to do the necessary services for this purpose as follows:-

1. Formation of the said Saudi Company with a capital sufficient to purchase Fifty percent (50%) of the First Party's contribution in the mining lease, and to pay its share needed in equity for the Al Masane mining project.
2. To finalize the required procedures towards issuance of the Industrial License from the Ministry of Industry and Electricity to bring the ore out of the mine and manufacture the same in Plant to be established in the said area near the mine.
3. To finalize the necessary procedures to obtain the loan requested from the Industrial Development Fund.
4. To apply for and receive loans from commercial banks necessary to finance the project.
5. To apply and obtain the Ministerial resolution of the Minister of Petroleum and Mineral Resources approving transference of the mining lease to the First Party and the above mentioned Saudi Company jointly and severally.

Therefore, the Two Parties agree as follows:-

FIRST:

The abovementioned recitals shall be considered as an integral part of this Agreement and constructor of the same.

SECOND:

The Parties shall fulfill the duties hereunder and draw a workplan from time to time to distribute the responsibilities and functions of each party to achieve the aim of this agreement.

THIRD:

Each Party shall keep the other one informed with all of his actions and contacts to avoid inconsistency and insure harmony between the Parties.

FOURTH:

The First Party acknowledges that upon execution of this Agreement the Second Party shall be the sole responsible and authorized person to perform abovementioned duties and that the First Party shall no longer be obligated by any similar to or contradictory with the above duties.

FIFTH: FEES

The First Party shall pay the fees to the Second Party divided as follows:-

TO THE LEGAL ADVISOR: NASIR ALI KADASAH

1. To Mr. Nasir Ali Kadasah the sum of US\$ 10,000/- (US Dollar Ten Thousand Only) upon issuance of the Industrial License of the project from the Ministry of Industry and Electricity.
2. To Mr. Nasir Ali Kadasah the sum of US\$ 10,000/- (US Dollar Ten Thousand Only) upon approval of the Industrial Development Fund to grant the requested loan to the Project.
3. The First Party shall grant Mr. Nasir Ali Kadasah with 1,025,000 (One Million Twenty Five Thousand) shares of its authorized unissued common stock without consideration plus the option to purchase 1,425,000 (One Million Four Hundred and Twenty Five Thousand) shares of its authorized unissued common stock for One Dollar per share and this right shall remain valid for Five (5) years from the date of registration of the Saudi Company. Such rights shall be apportioned as follows:-
 - a) The right to be granted and to purchase 15% (Fifteen percent) of all abovementioned shares upon issuance of Industrial License, i.e. a grant of 153,750 (One Hundred and Fifty Three Thousand Seven Hundred and Fifty) shares without consideration and the right to purchase 213,750 (Two Hundred and Thirteen Thousand Seven Hundred and Fifty) shares for one dollar per share.
 - b) The right to be granted and to purchase 25% (Twenty Five percent) of all abovementioned shares upon approval of the Industrial Development Fund to grant the requested loan; i.e. a grant of 256,250 (Two Hundred and Fifty Six Thousand Two Hundred and Fifty) shares without consideration and the right to purchase 356,250 (Three Hundred and Fifty Six Thousand Two Hundred and Fifty) shares for one dollar per share.
 - c) The right to be granted and to purchase 15% (Fifteen percent) of all abovementioned shares upon approval of the Commercial Banks of the requested loan; i.e. a grant of 153,750 (One Hundred and Fifty Three Thousand Seven Hundred and Fifty) shares without consideration and the right to purchase 213,750 (Two Hundred and Thirteen Thousand Seven Hundred and Fifty) shares for one dollar per share.
 - d) The right to be granted and to purchase 15% (Fifteen percent) of all abovementioned shares upon registration of the Saudi Company and payment - by its shareholders - of an amount US\$ 10,625,000 (US Dollar Ten Million Six Hundred and Twenty Five Thousand) to the First Party as a price of 50% (Fifty percent) of the First Party's share in the mining lease and payment of another amount of US\$ 13,000,000 (US Dollar Thirteen Million) as their contribution in the required capital of the project, i.e. a grant of 153,750 (One Hundred and Fifty Three Thousand Seven Hundred and Fifty) shares without consideration and the right to purchase 213,750 (Two Hundred and Thirteen Thousand Seven Hundred and Fifty) shares for one dollar per share.
 - e) The right to be granted and to purchase 30% (Thirty percent) of all abovementioned shares upon issuance of the Ministerial resolution from the Minister of Petroleum and Mineral Resources permitting the transference of ownership of the license to the First Party.

And the Saudi Company jointly and severally, i.e. a grant of

307,500 (Three Hundred and Seven Thousand Five Hundred) shares without consideration and 427,500 (Four Hundred and Twenty Seven Thousand Five Hundred) shares for one dollar against each share.

TO THE ECONOMIC ADVISOR: DAR AL KHALEEJ FOR RESEARCH AND ECONOMIC ADVICE

- 1) Dar Al Khaleej for Research and Economic Advice shall be paid the sum of US\$ 10,000/- (US Dollar Ten Thousand) upon issuance of the Industrial License from the Ministry of Industry and Electricity to the project.
- 2) The First Party shall grant Mr. Tawfiq Abdulaziz Al-Sowailim 975,000 (Nine Hundred and Seventy Five Thousand) shares of the First Party's authorized unissued common stock without consideration as well as a right to purchase 875,000 (Eight Hundred and Seventy Five Thousand) shares from the First Party's authorized unissued common stock for One Dollar per share and such right shall continue valid for a term of Five (5) years from the date of formation of the Saudi Company.

The above rights shall be apportioned only as follows:-

- a) The right to be granted and to purchase 15% (Fifteen percent) of all abovementioned shares upon issuance of the Industrial License, i.e. to grant 146,250 (One Hundred and Forty Six Thousand Two Hundred and Fifty) shares without consideration and the right to purchase 131,250 (One Hundred and Thirty One Thousand Two Hundred and Fifty) shares for one dollar per share.
- b) The right to be granted and to purchase 25% (Twenty Five percent) of all abovementioned shares upon approval of the Industrial Development Fund to grant the requested loan; i.e. to grant 243,750 (Two Hundred and Forty Three Thousand Seven Hundred and Fifty) shares without consideration and the right to purchase 218,750 (Two Hundred and Eighteen Thousand Seven Hundred and Fifty) shares for one dollar per share.
- c) The right to be granted and to purchase 15% (Fifteen percent) of all abovementioned shares upon approval of the Commercial Banks to grant the requested loan; i.e. 146,250 (One Hundred and Forty Six Thousand Two Hundred and Fifty) shares without consideration and the right to purchase 131,250 (One Hundred and Thirty One Thousand Two Hundred and Fifty) shares for one dollar per share.
- d) The right to be granted and to purchase 15% (Fifteen percent) of all abovementioned shares upon registration of the Saudi Company and payment - by its Shareholders - an amount of US\$ 10,625,000 (US Dollar Ten Million Six Hundred and Twenty Five Thousand) to the First Party as the price of 50% (Fifty percent) of the First Party's share in the mining lease and payment of another amount of US\$ 13,000,000 (US Dollar Thirteen Million) as their contribution in the required capital of the project, i.e. to grant 146,250 (One Hundred and Forty Six Thousand Two Hundred and Fifty) shares without consideration and the right to purchase 131,250 (One Hundred and Thirty One Thousand Two Hundred and Fifty) shares for one dollar per share.
- e) The right to be granted and to purchase 30% (Thirty percent) of all abovementioned shares upon issuance of the Ministerial resolution of the Minister of Petroleum and Mineral Resources permitting transference of the ownership of the mining lease to the First Party and the Saudi Company jointly and severally, i.e. to grant 292,500 (Two Hundred and Ninety Two Thousand Five Hundred) shares without consideration and the right to purchase 262,500 (Two Hundred and Sixty Two Thousand Five Hundred) shares for one dollar per share.

SIXTH:

Sale and grant of abovementioned shares shall be subject to the Rules of sale of such shares to non-Americans promulgated by Securities and Exchange Commission (Rule 144).

SEVENTH:

Duties of the First Party hereunder shall be subject to the approval of the Board of Directors of Arabian Shield Development Company and the First Party will provide the Second Party with a copy of the approval, within two weeks, if issued. In case such approval is not issued, then, this Agreement shall, automatically, be cancelled and the Second Party shall have no right to ask for any compensation.

EIGHTH:

The term of this Agreement shall be Twelve (12) months from the date of the Second Party's receipt of Arabian Shield Development Company's approval and receipt of all required documents to perform the duties of the Second Party - unless the delay caused by the First Party or agreement is reached by in writing by both parties to renew or extend this agreement.

NINTH:

If any dispute arise between the parties in relation to understanding or performance of this Agreement it shall be solved amicably. If this is not achieved then the dispute shall be referred to Arbitration according to Saudi Arbitration law.

The Second Party acknowledges that it shall not be entitled to any fees or compensation against his mentioned duties beyond the scope of the stages mentioned in this Agreement.

FIRST PARTY	SECOND PARTY
For: Arabian Shield Development Co. /s/ Hatem Hussein El-Khalidi	1. Nasir Ali Kadasah /s/ Nasir Ali Kadasah
by: Hatem Hussein El-Khalidi	2. Dar Al Khaleej for Research and Economic Advisors by Tawfiq Abdulaziz Al-Sowailim /s/ Tawfiq Abdulaziz Al-Sowailim

ARABIAN SHIELD DEVELOPMENT COMPANY
10830 North Central Expressway
Suite 175
Dallas, Texas 75231 U.S.A.

P.O. Box 1516, Jeddah 21441
Saudi Arabia
C.R. 4030097605 o C.C.J.45522

Administration Tel. { 642 6529
{ 643 5410
Technical Office Tel. { 667 3534
{ 669 0641
Fax: { 643 3410
{ 669 0641

3 March, 1997

Mr. Nasir Ali Kadasah
Dar Ali Khaleej for Research and Economic Advisors
Riyadh
Saudi Arabia

Gentlemen:

Reference is made to the "Financial And Legal Services And Advise Agreement", dated May 20, 1996. It is requested that certain texts in the

Agreement be changed to the following, to confirm with our present understanding:

Page 1, (4th Paragraph)

Whereas the First Party desires to participate with "The Saudi Company For Mining Industries" a Saudi Limited Liability Company "under formation", in which First Party shall own 50% of the stock of the said Company, while the other 50% shall be owned by Saudi Shareholders.

This Company shall apply to obtain an industrial license and finance the project, and shall apply to the Minister of Petroleum and Mineral Resources to transfer the mining Lease, now held by First Party to the "Saudi Company For Mining Industries"

Page 3 (fifth paragraph)

e) The right to be granted and to purchase 30% (thirty percent) of all above mentioned shares upon issuance of the Ministerial resolution from the Minister of Petroleum and Mineral Resources permitting the transference of the ownership of the mining lease to the Saudi Company For Mining Industries", i.e, a grant of 307,500 (three hundred and seven thousand five hundred) shares without consideration and the option to purchase 427,500 (Four hundred and twenty seven thousand five hundred) shares for one (1) dollar per share.

Page 5 (first paragraph)

a) the right to be granted and to purchase 30% (thirty percent) of all above mentioned shares upon issuance of the Ministerial Resolution of the Minister of Petroleum and Mineral Resources permitting transference of the ownership of the mining lease to the "Saudi Company For Mining Industries" i.e. a grant of 292,500 (two hundred and ninety two

ARABIAN SHIELD DEVELOPMENT COMPANY
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 { 669 0641

Fax: { 643 3410
 { 669 0641

Date: 3 March, 1997

- 2 -

thousand five hundred) shares without consideration and the option to purchase 262,500 (two hundred sixty two thousand five hundred) shares for one dollar per share.

Very truly yours

Arabian Shield Development Company

/s/ Hatem El-Khalidi

by: Hatem El-Khalidi, President

Agreed to:

Nasir Ali Kadasah

by:

/s/ Nasir Ali Kadasah

date:

15/3/97

Dar Al Khaleej For Research and Economic Advisors

by: /s/ Tawfiq Abdulaziz Al-Sowailim

date:

March 16th, 97

ARABIAN SHIELD
DEVELOPMENT COMPANY

ANNUAL REPORT TO STOCKHOLDERS
FOR THE YEAR ENDED DECEMBER 31, 1996

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, which was subsequently updated in 1996. The mining lease has an initial thirty (30) year term, with the Company having the option to renew or extend the term of the lease for additional periods not to exceed twenty (20) years. The Company will pay the Saudi Arabian government income taxes in accordance with the income tax law then in force, in accordance with Article 45 of the Mining Code (the current tax is now 45% of net income). However, in accordance with Article 46 of the Mining Code, such income tax will not be due in respect to mining operations during the period of five years starting from the date of the first sale of products or five years from the beginning of the fourth year after the issue of the mining lease, whichever occurs first.

Under the mining lease agreement, the Company is obligated, when actual profits are realized from its commercial mining operations in the Al Masane area, to form a Saudi public stock company in which the Company will own 50% of the shares, the Petroleum and Mineral Organization ("Petromin"), a company wholly owned by the Saudi Arabian government, will have the option to acquire up to 25% of the shares, and the remaining shares will be offered for public subscription to Saudi Arabian citizens. In the 1996 update to the 1994 full bank feasibility study of the Al Masane lease area, the independent mining consultants estimated the total capital costs of the Al Masane project to be \$88.6 million. The Company and its Saudi Arabian advisors are in the process of forming a Saudi limited liability company to own and operate the project, 50% of which will be owned by the Company and the remaining 50% of which will be owned by the Saudi Arabian investors. The Saudi Arabian investors will contribute 25% of the capital cost of the project. The Company believes that another 25% of the capital cost of the project may be obtained through loans from commercial banks, and that the remaining 50% of the capital cost of the project would come from an interest-free loan from the Saudi Industrial Development Fund ("SIDF"). To be eligible for an interest-free loan from the SIDF to fund 50% of the capital cost of the project, the Company together with its Saudi Arabian advisors obtained an industrial license from The Ministry of Industry and Electricity on December 3, 1996. The Company owns 50% of the license and the Saudi Arabian advisors the remaining 50%. When actual profits are realized from commercial mining operations of the project, the Saudi limited liability company will be transformed into a Saudi public stock company, 50% of the shares of which will be owned by the Company and the remaining shares of which will be owned by Petromin, up to 25%, and Saudi Arabian investors.

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.

Under the terms of the mining lease agreement, the Company agreed to pay in advance 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 (approximately \$117,300 annually) during the period of the lease for the total lease area of 44 square kilometers. The Company made rental payments for the first year of the lease. As of December 31, 1996, the Company has not paid for rentals of approximately \$309,000. It is contemplated that the Saudi limited liability company will assume responsibility for the rental payments and all arrearages.

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

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developed during the past ten years; incorporation of new mill designs and the latest water recycling methods; investigation into the shipping and marketing of zinc and copper concentrates; and an economic analysis of the project. The feasibility study contains specific recommendations to insure that the construction of the project is accomplished as expeditiously and economically as possible. Engineering design and costing of the project was done by Davy International of Toronto, Canada. The feasibility study cost the Company approximately \$1 million and was presented to the Company on July 22, 1994. The feasibility study was updated in July 1996.

The Al Masane ore is located in three mineralized zones known as Saadah, Al Houra and Moyeath. The diluted minable, proven and probable ore reserves at the

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

A review by WGM of the equipment and process flowsheet contained in the 1982 feasibility study prepared by WGM indicated that new technology developed during the past ten years could be used to reduce the capital cost and improve the metallurgical recoveries. In particular, the use of semi-autogenous grinding to reduce the capital cost of the grinding section and developments in reagents were believed to hold the greatest potential for improving the economics 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 economics of the cyanidation of the zinc concentrate and tailings in order to improve gold and silver recoveries found gold and silver recoveries to range from 50% to 77%. To recover gold and silver from the zinc concentrate and tailings, WGM recommended that a cyanidation plant be included in the process flowsheet. Dore bullion would be produced. WGM concluded that the inclusion of a cyanidation plant would make a positive contribution to the economics of the project under the base conditions.

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

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

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of gold and silver. These concentrates are estimated to be 22,000 ounces of gold and 800,000 ounces of silver and will be sold to copper and zinc custom smelters and refineries worldwide.

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

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

The base case assumes the corporate structure of the entity to be formed to operate the project, currently planned to be a Saudi limited liability company, will be owned 50% by the Company and 50% by Saudi Arabian investors and that the owners of this entity would contribute an aggregate of \$21.2 million to the cost of the project. The base case further assumes financing for the project from commercial loans in the aggregate amount of \$21.2 million bearing interest at the rate of 8% per year and a loan in the amount of \$43.8 million from the SIFD repayable in equal annual installments over the initial life of the mine. The

remainder of the project financing would be contributed by cash generated by the operation of the project. The base case assumes that the \$11 million loan outstanding to the Saudi Arabian government will be paid by the Company in accordance with a repayment schedule to be agreed upon with the Saudi Arabian government. Based on these assumptions, and assuming the average prices of metal over the life of the mine to be \$1.05 per pound for copper, \$.60 per pound for zinc, \$400 per ounce of gold and \$6.00 per ounce of silver, WGM's economic analysis of the base case shows the project will realize an internal rate of return of 13.1%, the Company's and the Saudi Arabian investors' internal rates of return would be 27.3% and 12.1%, respectively, and projected net cash flow from the project of \$95.1 million. The 1994 feasibility study base case showed the project would realize a 14.05% internal rate of return. Cash flow under the base case is exclusive of income tax as the base case assumes that any such tax would be paid by individual investors and not by the project. Assuming a 10% discount rate, the net present value of the project as shown in the update is \$12.16 million compared to the \$15.5 million net present value of the project shown in the 1994 feasibility study. Based on the update, WGM believes that the economic analysis shows that the project remains viable.

The Company retained Carlyle SEAG ("Carlyle"), of Washington, D.C. and Saudi Arabia, on March 27, 1995 as the Company's financial advisor in connection with the Al Masane mining project. On March 13, 1996, the agreement with Carlyle was effectively terminated by mutual consent. A new financial and legal services was signed on May 20, 1996. See "Management's Discussion and Analysis of Financial Condition and Results of Operations."

On September 30, 1995, the Company made a formal application to the SIDF for an interest-free loan to fund 50% of the capital cost of the Al Masane project. The 1994 feasibility study was submitted to the SIDF together with the application. The SIDF informed the Company that in order to be eligible for a loan, the Company and its Saudi Arabian advisors had to obtain an industrial license for the project from The Ministry of Industry and Electricity. An industrial license was issued on December 3, 1996. The industrial license and the 1996 update to the feasibility study were presented to the SIDF on December 23, 1996. As required by the SIDF, the Company is preparing, through its engineering consultants, bid documents to be given to three bidders who have been qualified to construct the plants and infrastructure of the

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project. The Company anticipates that these bid documents will be completed before April 15, 1997. See "Management's Discussion and Analysis of Financial Condition and Results of Operations."

On May 15, 1991, the Company filed a complaint with the U.S. Department of Justice ("DOJ") against Hunt Oil Company of Dallas, Texas ("Hunt"), alleging violations of the Foreign Corrupt Practices Act ("FCPA") by Hunt in obtaining its Petroleum Production Sharing Agreement ("PSA") in Yemen in 1981, subsequent to the Company presenting a bid to the Yemen government for the same area before Hunt made its application. The Company's Washington, D.C. attorneys opined that, because the PSA of Hunt is still ongoing, and under its auspices, payments and receipts occur daily, the DOJ still has jurisdiction to continue its investigation. A letter from the DOJ on December 19, 1995 stated its interest in receiving additional documentation regarding the Company's allegations. On February 28, 1996, the Company sent more documents to the DOJ which it believed further supported its allegations. The Company's Washington, D.C. attorneys opined also that the Victim Restitution Act provides for restitution to the Company of monies lost as a result of the alleged wrongdoing by Hunt, if Hunt is convicted under the FCPA. A letter from the DOJ dated October 1, 1996 stated that the documents presented did not suggest any criminal events occurred within the statute of limitations, and that, at that time, the DOJ did not intend to pursue the investigation. On November 18, 1996, legal counsel retained by the Company, after studying the facts of the case, sent the DOJ an analysis concluding that while the statute of limitations of FCPA may have lapsed, the statute of limitations for conspiracy to violate the FCPA had not lapsed, and that, as a consequence, the DOJ could criminally prosecute Yemen Hunt for conspiracy to violate the FCPA. The Company's legal counsel met with the Fraud Section of the DOJ on December 13, 1996 and were told that the DOJ would take a more aggressive stance if more information of evidentiary quality were presented to the DOJ. The Company intends to vigorously pursue obtaining such further information in the United States and in Yemen.

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

statute of limitations period under Yemen criminal law had run, Yemen Hunt could not be prosecuted for criminal libel. The Company intends to vigorously pursue the matter under the civil libel laws of Yemen.

The Company owns, through a wholly owned subsidiary, South Hampton Refining Company, of Silsbee, Texas which owns and operates a special products refinery which produces pure pentanes and hexanes and other specialty chemicals for the plastics industry. Total gross revenues for 1996 for the refinery were approximately \$21.4 million and the cash flow realized was approximately \$655,000. It is significant that the plant sells about 40% of all pentanes consumed in the United States.

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

Respectfully submitted,

John A. Crichton
Chairman of the Board

Hatem El-Khalidi
President and Chief Executive
Officer

March 28, 1997

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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 the 1996 update to the 1994 bankable feasibility study conducted by an independent mineral consulting firm indicate that the proposed Al Masane mining operation is economically viable.

National Mining Company, a private Saudi company ("National Mining"), which previously had a 50% interest in the joint venture formed to explore and develop the Al Masane area, relinquished its rights to the mining lease and assigned them to the Company. The Company was granted exploration licenses for the Wadi Qatan and Jebel Harr areas in southwestern Saudi Arabia, approximately 30 kilometers east of the Al Masane area, in 1971 and 1977, respectively. The exploration licenses by their terms have expired. The Company has been orally advised by Saudi Arabian government officials that the licenses will be extended as long as mineral exploration is being conducted on the areas which they cover, although there can be no assurance that the Company's license rights will be honored. Although the expired exploration licenses for Wadi Qatan and Jebel Harr were awarded jointly to the Company and National Mining, the exploration work on the licensed areas has been carried on exclusively by the Company. Pursuant to an agreement among the Company, National Mining and the Petroleum and Mineral Organization ("Petromin"), the official mining and petroleum company of the Saudi Arabian government, which governed the rights of the parties if an exploration license was converted into a mining lease, National Mining's rights in these jointly held expired exploration licenses entailed responsibilities of joint exploration expenditures which National Mining did not want to assume. For this reason, National Mining has orally advised the Company that it has relinquished its rights in all other areas in Saudi Arabia and assigned them to the Company. No consideration was paid by the Company to National Mining for the relinquishment of National Mining's rights in all other areas of Saudi Arabia. The Company remains a party to the agreement with Petromin notwithstanding National Mining's relinquishment of its rights. When financing for the Al Masane project is completed, the Company plans to make an application for an expanded exploration license for an area of approximately 2,800 square kilometers which includes the original Greater Al Masane area and the Wadi Qatan and Jebel Harr areas.

In May 1993, the Company had discussions with Chevron Chemical Company regarding the Company's proposal to purchase 5,000 barrels per day of mixed pentanes from an Aromax(R) petrochemical project to be built in Jubail, Saudi Arabia by Chevron Chemical in a joint venture with Saudi Venture Capital Group (SVCS). The Company and some Saudi partners, all of whom are directors and/or stockholders of the Company, plan to form a Saudi limited liability company which will build

and manage a processing plant located next to the Aromax(R) plant in Saudi Arabia. The Company would have a 25% interest in the limited liability company and would manage the plant. The plant will be similar to the South Hampton refinery in producing purified pentanes from a feedstock of mixed pentanes obtained from the Aromax(R) plant. Chevron Chemical advised the Company by letter in July 1993 that Chevron Chemical and SVCS have jointly agreed to commit to supply the proposed pentane project with up to 5,000 barrels per day of mixed pentane feedstock. Engineering and marketing studies of the project made in 1994 by outside consultants reflected positive results. Planning then began toward the construction and operation of the Aromax(R) plant and the processing plant but was delayed during 1995 because of the absence of a firm commitment for the feedstock supply to the Aromax(R) plant. The Aromax(R) plant received final approval

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from the Saudi Arabian government in March 1996 and the Company and its Saudi partners, following the confirmation of their agreement with Chevron Chemical, are preparing an application for an industrial license from the Ministry of Industry to build the processing plant. The application will be submitted in the near future.

In December 1993, the Company commissioned Sherritt Ltd. of Fort Saskatchewan, Canada, to prepare a conceptual engineering design for a proposed zinc refinery based on Sherritt's two stage pressure leach process, to be built by the Company and Saudi partners at the Red Sea port of Yanbu, Saudi Arabia. The refinery would have the capacity to produce 100,000 tonnes of slab zinc per year, with elemental sulfur as a by-product. Sherritt Ltd. completed the study in May 1994 which contains a proposed flow sheet that has been commercialized and designed for a state of the art zinc refinery. Sherritt's zinc pressure leach technology provides significant advantages over other existing zinc production processes, including having the reputation as the most favored technology for environmental considerations. In its study, Sherritt concluded, after considering all of the presently identifiable elements, that they offer a strong potential for the project and enhance the concept. Sherritt encouraged the Company to carry out further studies toward the implementation of the project. There has been a recent inquiry about this project from a zinc smelting and refining company in Asia.

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

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

The Company owns all of the capital stock of a coal company which does not presently own or hold any mineral interests and is presently inactive. The coal company had a net operating loss carryforward of approximately \$5.9 million at December 31, 1996. The Company has had negotiations with several companies toward the possible use of the Coal Company's carryforward amount, but no agreements have been 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 1996 and 1995, respectively, as reported by NASDAQ.

<TABLE>
<CAPTION>

	1996				1995			
	1st	2nd	3rd	4th	1st	2nd	3rd	4th
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
High	3 3/4	3 3/8	2 5/8	2 3/32	2 3/8	2 3/8	1 7/8	1 1/4
Low	1/4	1 1/2	1 1/2	1 5/8	1 3/4	1 5/8	5/8	5/8

At March 17, 1997, there were 900 record holders of the Company's Common Stock. The Company has not paid a dividend since its inception.

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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>

	1996	1995	1994	1993	1992
<S>	<C>	<C>	<C>	<C>	<C>
Revenues.....	\$22,014	\$18,359	\$17,765	\$15,267	\$13,468
Net Income (Loss).....	\$ (391)	\$ (369)	\$ 2,852	\$ (1,338)	\$ (2,196)
Net Income (Loss) Per Share.....	\$ (.02)	\$ (.02)	\$.14	\$ (.08)	\$ (.14)
Total Assets (at December 31).....	\$44,096	\$40,805	\$41,057	\$41,090	\$38,729
Notes Payable (at December 31).....	\$11,376	\$15,086	\$15,945	\$18,044	\$18,571
Total Long-Term Obligations (at December 31).....	\$ 4,423	\$ 1,676	\$ 1,148	\$ 908	\$ 889

</TABLE>

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

With the exception of revenues generated by the operations of the refinery, 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 1996, the Company took certain actions designed to generate additional equity capital and improve its financial condition, including: (i) the negotiation by South Hampton Refining Company, an indirect wholly owned subsidiary of the Company ("South Hampton"), of an Amended and Restated Credit Agreement with Den norske Bank ASA, amending and restating the then outstanding credit agreement to provide for a revolving credit facility in an aggregate principal amount of up to \$1,965,000; (ii) the restructuring of certain indebtedness of South Hampton owed to Saudi Fal Co., Ltd., a limited liability company owned by a stockholder of the Company ("Saudi Fal"), and American Shield Refining Company, a wholly owned subsidiary of the Company (the "Refining Company"), pursuant to promissory notes in the original principal amounts of \$1,945,773.49 and \$1,694,605.08, respectively, which promissory notes are subordinated to the Amended and Restated Credit Agreement with Den norske Bank ASA; (iii) approval by the Company's Board of Directors in June 1996 of the sale of up to 1 million shares of the Company's Common Stock through private placements at a price no less than \$1.00 per share; (iv) the sale of 450,000 shares of the Company's Common Stock at \$1.00 per share to a Saudi Arabian investor who is a stockholder of the Company and approval of the sale of an additional 450,000 shares of the Company's Common Stock at \$1.00 per share to the same investor, the purchase price for such additional shares being payable in monthly installments of \$100,000; and (v) approval of the sale of 50,000 shares of the Company's Common Stock to a Saudi Arabian investor.

The exploration licenses held by the Company for the Wadi Qatan and Jebel Harr areas in Saudi Arabia, by their terms, have expired, although officials of the Saudi Arabian government have provided verbal assurance to the Company that the licenses will be extended as long as exploratory work is being carried out on the areas which they cover. None of the related projects at Al Masane or the other interests in Saudi Arabia were being developed at December 31, 1996 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

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

To assist the Company in obtaining financing for the project, on March 27, 1995, the Company retained Carlyle SEAG of Washington, D.C. ("Carlyle") as the Company's financial advisor. On March 13, 1996, the agreement with Carlyle was terminated by mutual consent after Carlyle informed the Company that it had to withdraw as the Company's financial advisor because of a conflict of interest since the Carlyle Group, which owns Carlyle, advises the Saudi Arabian government on its offset program.

After the agreement with Carlyle was terminated, on May 20, 1996, the Company entered into a Financial and Legal Services and Advice Agreement with Nasir Ali Kadasah, for legal advice, and Dar Al Khaleej, a Saudi Arabian consulting

company, for research and economic advice. The purpose of this agreement is for the two Saudi Arabian advisors to assist the Company in obtaining financing for the Al Masane project. To this end, the agreement contemplates that the Saudi Arabian advisors will perform the following:

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

The agreement provides that the Saudi Arabian advisors are solely responsible for the performance of the foregoing obligations and that the Company has no obligation therefor.

As consideration for performing these obligations, the Company has agreed to pay Mr. Kadasah and Dar Al Khaleej \$10,000 each upon the issuance of the industrial license and Mr. Kadasah \$10,000 upon approval of the loan by the SIDF. The Company has also agreed to issue to Mr. Kadasah and Mr. Tawfiq Abdulaziz Al-Sowailim, as agent for Dar Al Khaleej, up to 1,025,000 and 975,000 shares of the Company's Common Stock, respectively, and to grant Mr. Kadasah and Mr. Tawfiq Abdulaziz Al-Sowailim, as agent for Dar Al Khaleej, options to purchase up to 1,425,000 and 875,000 shares of the Company's Common Stock, respectively. The Company is obligated to issue such shares and grant such options in designated amounts upon completion of each of the foregoing obligations. The issuance of the shares would be for consideration consisting solely of services rendered to the Company. The options are immediately exercisable on the date of grant, have a five-year term commencing on the date of formation of the Saudi limited liability company and an exercise price of \$1.00 per share.

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

Pursuant to the mining lease agreement, when the profitability of the project is established, the Company is obligated to form a Saudi public stock company with Petromin. 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. Title to the mining lease

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and the other obligations specified in the mining lease will be transferred to the Saudi public stock company. Responsibility for the repayment of the \$11 million loan from the Saudi Arabian government will remain with the Company. In December 1994, the Company received instructions from the office of the Minister of Petroleum and Mineral Resources stating that it is possible for the Company to form a Saudi company without Petromin but that the sale of stock to the Saudi public could occur only after two years of profits from commercial operations of the mine. The instructions added that Petromin will still have the right to purchase shares in the Saudi public stock company any time it desires.

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

principal on any debt owed by South Hampton to Saudi Fal or the Company. The Credit Agreement is secured by all of the assets of South Hampton and Gulf State Pipe Line Company, Inc., a wholly owned subsidiary of South Hampton ("Gulf State"), and all of the issued and outstanding shares of TOCCO, South Hampton and Gulf State. South Hampton is required to collect all receivables through a cash collateral account at a local bank. South Hampton was not in compliance with a certain financial covenant as of December 31, 1996, which noncompliance has been waived by the Bank.

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

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

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aromatic compounds, which was part of the reason the refinery participated in the Aromax(R) development project initially.

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

RESULTS OF OPERATIONS

COMPARISON OF THE YEARS 1996 TO 1995

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

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

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

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

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

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in the toll processing business for over 30 years and has a good reputation in the industry for this type of work. Management intends to expand the refinery's involvement in this area as opportunities arise.

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

The equity in losses of affiliate in 1995 and 1994 was attributable to the cost of maintaining the Nevada mining properties of Pioche Ely Valley Mines, Inc. ("Pioche"). In 1996, the Company concluded that its voting control of Pioche was no longer temporary and, therefore, the asset and liability amounts of Pioche have been consolidated into its financial statements. The minority interest in 1996 of \$13,072 represents the Pioche minority shareholders portion of Pioche's 1996 loss. There has been no activity in several years on the Pioche properties primarily due to the lack of financing for claims to be explored and developed. Interest income in 1996 and 1995 was from the investment of temporary excess cash in time deposits in Saudi Arabia and a short-term investment by the refinery. In 1996 and 1995, there was no operating activity on any of the Saudi Arabia mining properties. Assuming financing can be obtained, the results of the 1996 update to the 1994 feasibility study contemplate that construction of an ore treatment plant and all infrastructure for a mining facility at Al Masane is estimated to take 18 months to complete at an estimated cost of \$88.6 million, an increase of \$7.3 million over the 1994 study estimate.

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

Primarily as a result of the Company's write-off of its total investment in the coal leases in 1988, the Company had net operating loss carryforwards of approximately \$33.3 million at December 31, 1996, of which approximately \$5.9 million is limited to any future net income of the coal company and approximately \$1.7 million is limited to any future net income of the refinery. These carryforwards expire during the years 1997 through 2010. The Company has had negotiations with several companies toward the possible use of the coal company's carryforward amount, but no agreements have been reached.

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

COMPARISON OF THE YEARS 1995 TO 1994

During the fiscal year ended December 31, 1995, the Company had a net loss of \$369,232 compared to net income of \$2,852,306 for the fiscal year ended December 31, 1994.

The gross refined product sales in 1995 of \$17,741,862 was an increase of \$177,636 from 1994 while the cost of sales in 1995 of \$15,575,054 was an increase of \$1,824,304 from 1994, resulting in a net margin decrease in 1995 of \$1,646,668. After processing fee income, general and administrative expenses and depreciation and amortization, the operating loss of the Company in 1995 of \$266,236 was \$2,571,862 less than the operating income in 1994 of \$2,305,626. The net income for the refinery in 1995 of \$359,605 was \$3,154,593 less than the net income in 1994 of \$3,514,194. Two refining company items contributed to the higher income in 1994: (i) operating income included \$975,000 relating to the reversal of a charge in 1992 for potential expenses relating to litigation that was settled in

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1994; and (ii) an extraordinary income item of \$578,150 attributable to the settlement of an indebtedness owed to a vendor.

The refinery's net income in 1995 reflected the steady demand which the plastics industry experienced toward the end of 1994 and throughout 1995. Most of 1994 could be characterized as a period of rising prices, pent-up demand and high operating utilization rates with strong gross margins on feedstock costs. In comparison, the refinery's 1995 results reflect a 3% decrease in sales volume, from 21,430,000 gallons in 1994 to 20,798,000 gallons in 1995, and a 43% reduction in gross margins. The refinery's sales continued to be solid with the majority of its products continuing to be placed into the higher priced specialty markets. Several new customers were added during 1995 and product sales attained a reasonable level of performance. The ability of the refinery to produce the highest quality products available in its field has enabled it to remain competitive even during the periods of low demand or high feedstock prices.

The primary feedstock of the refinery, natural gasoline, is the heavier liquid produced by natural gas processing plants and by LPG fractionators. Feedstock prices in 1995 were approximately 23% higher than in 1994 resulting in reduced gross margins. The chemical industry, primarily the ethylene crackers, continued to be a big user of natural gasoline in 1995 which contributed to the higher feedstock prices. Feedstock prices are expected to sustain 1995 levels throughout most of 1996.

The refinery has experienced a healthy growth in its toll processing business over the last three years and expects the opportunities to continue to develop, although there can be no assurances to that effect. Toll processing fees were \$163,977, \$200,757 and \$616,796 in 1993, 1994 and 1995, respectively. The increase in the toll processing business is indicative of the direction of the refining and petrochemical industries in the U.S. Many larger companies are "rightsizing" and outsourcing smaller jobs and processes which might have been formerly managed in their own facilities. The refinery has been in the toll processing business for over 30 years and has a good reputation in the industry for this type of work. Management intends to expand the refinery's involvement in this area as opportunities arise.

General and administrative expenses increased by \$336,213 to \$2,372,683 in 1995 from \$2,036,470 in 1994. This increase was mostly attributable to higher payroll, franchise tax, insurance and regulatory expenses at the refinery and stock option expense incurred in 1995 by the Company. The expenses of regulatory compliance and reporting continued to increase. Interest expense, which was practically all attributable to the debt of the refinery, increased slightly by \$22,182 from \$347,364 in 1994 to \$369,546 in 1995. This increase was primarily due to higher interest rates in 1995.

The equity losses of affiliate in 1995 of \$24,112 represented a decrease of \$120,348 from 1994 and was applicable to the cost of maintaining the Nevada mining properties of Pioche. The 1994 loss was higher than usual due to an increased loss experienced by Pioche on the write-off of several unpatented claims that were considered to have no future value. There was no activity in 1995 and 1994 on the Pioche properties primarily due to the lack of financing for claims to be explored and developed. Interest income in 1995 and 1994 was from the investment of excess cash in time deposits in Saudi Arabia and a short-term investment by South Hampton. In 1995 and 1994, there was no operating activity on any of the Saudi Arabia mining properties. Assuming financing can be obtained, the results of the 1994 feasibility study contemplate that construction of an ore treatment plant and all infrastructure for a mining facility at Al Masane is estimated to take 18 months to complete. The 1994 feasibility study estimated the cost of the mining facility to be \$81.3 million.

Miscellaneous income represents various items of other income which individually are not significant enough to warrant being separately disclosed. Miscellaneous income in 1994 included \$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 miscellaneous income are tank rentals, building rentals, cancellation of debt income, commission income and occasionally small asset sale proceeds. In 1995 and 1994, the refinery received \$101,640 each year from the leasing of an office building. Tank rentals decreased from \$97,000 in 1994 to \$78,000 in 1995 due to a change in lessees and a decrease in the rental rate.

Board of Directors and Stockholders
Arabian Shield Development Company

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

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit

also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above, present fairly, in all material respects, the consolidated financial position of Arabian Shield Development Company and Subsidiaries as of December 31, 1996, and the consolidated results of their operations and their consolidated cash flows for the year then ended, in conformity with generally accepted accounting principles.

The accompanying financial statements have been prepared assuming the Company will continue as a going concern. As discussed in Note 2 to the financial statements, the Company's sources of cash flow in 1996 were the operations of its refinery and the proceeds from the sale of common stock. Cash flow from the refinery is dedicated to repaying debt and funding refinery operations. As discussed in Notes 5 and 7 to the financial statements, the majority of the Company's assets consist of costs related to the acquisition, exploration, and development of mineral interests in Saudi Arabia. The ability of the Company to develop these properties is dependent upon obtaining additional financing. As discussed in Note 9, the Company is obligated to the Saudi Arabian government for a loan in the amount of \$11,000,000. The Company does not currently have the financial resources to pay this obligation and is attempting to reschedule the payment. Management's plans with regard to these matters are discussed in Note 2. These matters raise substantial doubt about the Company's ability to continue as a going concern. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

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

GRANT THORNTON LLP

Dallas, Texas
March 14, 1997

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, 1995 and the results of their operations and their cash flows for each of the two years in the period ended December 31, 1995, in conformity with generally accepted accounting principles. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our 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 5 and 7 to the financial statements, a substantial portion of the Company's total assets is comprised of mineral acquisition, exploration and development costs relating to its interests in Saudi Arabia which have been deferred at December 31, 1995. None of the related projects have been developed for commercial operation as of December 31, 1995, and significant expenditures, for which the Company must obtain financing, will be necessary before commercial operations, if any, are commenced.

As described in Note 10 to the financial statements, the Company is in default on repayment of an \$11 million loan from the Saudi Arabian government which was made to the Al Masane Project. The Company is attempting to reschedule payment of the loan.

As described in Notes 5 and 10 to the financial statements, the Company's refining subsidiary, South Hampton Refining Company ("South Hampton"), has short-term notes payable and current portions of long-term obligations totaling \$3.8 million. South Hampton does not have the ability to fully repay these current obligations from internally generated funds. Arabian Shield Development Company has not guaranteed the debt obligations of South Hampton. The Company's financial statements do not include any adjustments that might be necessary

should South Hampton be unable to satisfy its current obligations in an orderly manner.

PRICE WATERHOUSE LLP

PRICE WATERHOUSE LLP

Dallas, Texas
March 25, 1996

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

<TABLE>
<CAPTION>

ASSETS	December 31,	
	1996	1995
<S>	<C>	<C>
CURRENT ASSETS		
Cash and cash equivalents in United States	\$ 209,251	\$ 302,039
Short-term investments	298,726	294,610
Accounts receivable (net of allowance for doubtful accounts of \$168,484 in 1996 and \$145,709 in 1995)	2,643,691	1,791,821
Inventories	565,346	430,732
Total current assets	3,717,014	2,819,202
CASH IN SAUDI ARABIA	176,039	396,809
REFINERY PLANT, PIPELINE AND EQUIPMENT - AT COST	5,758,852	5,563,776
LESS ACCUMULATED DEPRECIATION	2,911,823	2,557,454
REFINERY PLANT, PIPELINE AND EQUIPMENT, NET	2,847,029	3,006,322
AL MASANE PROJECT	32,882,838	30,897,883
OTHER INTERESTS IN SAUDI ARABIA	2,431,248	2,431,248
MINERAL PROPERTIES IN THE UNITED STATES	1,418,615	--
INVESTMENT IN AND ADVANCES TO PIOCHE-ELY VALLEY MINES, INC	--	239,032
GOODWILL	117,598	397,902
OTHER ASSETS	505,566	617,019
TOTAL ASSETS	\$44,095,947	\$40,805,417

</TABLE>

The accompanying notes are an integral part of these statements.

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ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS - CONTINUED

<TABLE>
<CAPTION>

LIABILITIES AND STOCKHOLDERS' EQUITY	December 31,	
	1996	1995
<S>	<C>	<C>
CURRENT LIABILITIES		
Accounts payable	\$ 1,408,677	\$ 674,641
Accrued liabilities	520,445	617,995
Accrued liabilities in Saudi Arabia	1,174,229	1,011,980
Notes payable	11,375,780	15,086,191
Current portion of long-term debt	992,729	78,090
Current portion of long-term obligations	150,904	20,285
Total current liabilities	15,622,764	17,489,182
LONG-TERM DEBT	3,544,112	708,534

LONG-TERM OBLIGATIONS	35,009	185,875
ACCRUED LIABILITIES IN SAUDI ARABIA	714,143	636,047
DEFERRED REVENUE	129,685	145,189
COMMITMENTS AND CONTINGENCIES	--	--
MINORITY INTEREST IN CONSOLIDATED SUBSIDIARY	1,003,590	--
STOCKHOLDERS' EQUITY		
Common stock, authorized 40,000,000 shares of \$.10 par value: issued and outstanding, 20,956,494 shares in 1996 and 20,206,494 shares in 1995	2,095,649	2,020,649
Additional paid-in capital	34,932,700	33,210,750
Receivables from stockholders	(126,000)	(126,000)
Accumulated deficit	(13,855,705)	(13,464,809)
	-----	-----
Total stockholders' equity	23,046,644	21,640,590
	-----	-----
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 44,095,947	\$ 40,805,417
	=====	=====

</TABLE>

The accompanying notes are an integral part of these statements.

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ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

For the three years ended December 31, 1996

<TABLE>
<CAPTION>

	1996	1995	1994
	-----	-----	-----
<S>	<C>	<C>	<C>
Revenues			
Refined product sales	\$ 21,367,438	\$ 17,741,862	\$ 17,564,226
Processing fees	646,848	616,796	200,757
	-----	-----	-----
	22,014,286	18,358,658	17,764,983
Operating costs and expenses			
Cost of refined product sales and processing	19,357,737	15,575,054	13,750,750
General and administrative	2,284,422	2,372,683	2,036,470
Depreciation and amortization	693,251	677,157	647,137
Litigation	--	--	(975,000)
	-----	-----	-----
	22,335,410	18,624,894	15,459,357
	-----	-----	-----
Operating income (loss)	(321,124)	(266,236)	2,305,626
Other income (expense)			
Interest income	25,310	33,395	56,491
Interest expense	(336,979)	(369,546)	(347,364)
Minority interest	13,072	--	--
Equity in losses of affiliate	--	(24,112)	(114,460)
Miscellaneous income	228,825	257,267	443,836
	-----	-----	-----
Income (loss) before income taxes and extraordinary item	(390,896)	(369,232)	2,314,129
Income tax expense	--	--	(39,973)
	-----	-----	-----
Income (loss) before extraordinary item	(390,896)	(369,232)	2,274,156
Extraordinary item	--	--	578,150
	-----	-----	-----
Net income (loss)	\$ (390,896)	\$ (369,232)	\$ 2,852,306
	=====	=====	=====
Per common share			
Income (loss) before extraordinary item	\$ (0.02)	\$ (0.02)	\$ 0.11
Extraordinary item	--	--	0.03
	-----	-----	-----
Net income (loss)	\$ (0.02)	\$ (0.02)	\$ 0.14
	=====	=====	=====

Weighted average number of common shares outstanding	20,286,208	20,030,434	20,027,881
	=====	=====	=====

</TABLE>

The accompanying notes are an integral part of these statements.

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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>
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 sold	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
Common stock and common stock subscriptions sold	278,000	27,800	250,200	--	--	278,000
Payment on stockholder receivables	--	--	--	50,000	--	50,000
Write-off of stockholder receivable	(100,000)	(10,000)	(90,000)	100,000	--	--
Stock options issued	151,431	151,431	--	--	--	--
Net loss	--	--	--	--	(369,232)	(369,232)
December 31, 1995	20,206,494	2,020,649	33,210,750	(126,000)	(13,464,809)	21,640,590
Common stock sold	450,000	45,000	405,000	--	--	450,000
Common stock issued for services	300,000	30,000	520,000	--	--	550,000
Stock options issued	--	--	796,950	--	--	796,950
Net loss	--	--	--	--	(390,896)	(390,896)
December 31, 1996	20,956,494	\$ 2,095,649	\$ 34,932,700	\$ (126,000)	\$ (13,855,705)	\$ 23,046,644

</TABLE>

The accompanying notes are an integral part of this statement.

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ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

For the three years ended December 31, 1996

<TABLE>

<CAPTION>

	1996	1995	1994
	<C>	<C>	<C>
<S>			
Operating activities			
Net income (loss)	\$ (390,896)	\$ (369,232)	\$ 2,852,306
Adjustments for non-cash transactions			
Depreciation and amortization	693,251	677,157	647,137
Equity in losses of affiliate	--	24,112	144,460
Stock options issued	--	151,431	--
Extraordinary item	--	--	(578,150)
Effects of changes in			
Decrease (increase) in accounts receivable	(845,570)	(388,839)	101,134
Decrease (increase) in inventories	(134,614)	40,342	175,965
Decrease in other assets	135,287	87,016	30,052
(Decrease) increase in accounts payable and accrued liabilities	454,810	(267,830)	(821,334)
Decrease in deferred revenue	(15,504)	(15,504)	(15,504)
Other	(70,529)	(12,190)	(82,078)

Net cash provided by (used for) operating activities	(173,765)	(73,537)	2,453,988
Investing activities			
Additions to short-term investments	(4,116)	(291,915)	(243,770)
Proceeds from sale of short-term investments	--	255,787	--
Additions to Al Masane Project	(451,110)	(785,751)	(743,709)
Additions to refinery plant, pipeline and equip	(195,076)	(153,235)	(279,122)
Decrease in cash in Saudi Arabia	220,770	34,167	1,257,042
Increase (decrease) in accrued liabilities in Saudi Arabia	53,450	276,366	(105,276)
Net cash used for investing activities	(376,082)	(664,581)	(114,835)
Financing activities			
Common stock issued for cash	450,000	--	--
Decrease in receivables from stockholders	--	50,000	50,000
Additions to notes payable and long-term obligations	445,773	721,000	--
Reduction of notes payable and long-term obligations	(438,714)	(809,192)	(1,429,632)
Net cash provided by (used for) financing activities	457,059	(38,192)	(1,379,632)
Net increase (decrease) in cash	(92,788)	(776,310)	959,521
Cash and cash equivalents at beginning of year	302,039	1,078,349	118,828
Cash and cash equivalents at end of year	\$ 209,251	\$ 302,039	\$ 1,078,349

</TABLE>

The accompanying notes are an integral part of these statements.

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ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - BUSINESS AND OPERATIONS OF THE COMPANY

Since its organization on May 4, 1967, the principal activity of Arabian Shield Development Company (the "Company") has been the exploration and development of mineral deposits in Saudi Arabia (Note 7). In February 1986, the Company purchased all of the issued and outstanding capital stock of Dorchester Coal Company, which was subsequently renamed American Shield Coal Company (the "Coal Company") and is currently dormant. The Company, through its wholly-owned subsidiary American Shield Refining Company (the "Refining Company"), owns all of the outstanding common stock of Texas Oil and Chemical Company II, Inc. ("TOCCO"). South Hampton Refining Company ("South Hampton") is a wholly-owned subsidiary of TOCCO, and Gulf State Pipe Line Company, Inc. ("Gulf State") is a wholly-owned subsidiary of South Hampton. The principal assets of TOCCO and its subsidiaries are a specialty products refinery located outside of Beaumont, Texas, which currently processes light naphtha feedstock, and 50 miles of natural gas and product pipelines which connect the refinery to supplies and a marine terminal on the Gulf of Mexico. The Company also owns 46% of Pioche-Ely Valley Mines, Inc. ("Pioche") which owns mineral deposits in Nevada (Note 8). Pioche is consolidated for financial statement purposes at December 31, 1996.

NOTE 2 - GOING CONCERN

The accompanying consolidated financial statements have been prepared assuming the Company will continue as a going concern. The Company's sources of cash flow in 1996 were the operations of South Hampton and the proceeds from a stock sale to a Saudi Arabian investor. The Company is not currently generating cash flow from any other activities. As the cash flow attributable to South Hampton is fully dedicated to repayment of debt and funding of refinery operations (described in Note 9), the cash flow attributable to South Hampton currently is not adequate to support the Company's operations. As described in Note 9, the Company is liable to the Saudi Arabian government for an \$11,000,000 loan. The Company does not currently have the financial resources to pay this obligation.

Management plans to fund future operations initially through sales of its common stock and borrowings. It is expected that the operations and obligations of the Company will be eventually funded from operations of the Al Masane mine. However, because of uncertainties with respect to future sales of common stock, obtaining suitable financing, and reaching an

agreement on the repayment of the loan to the Saudi Arabian government, there is substantial doubt about the Company's ability to continue as a going concern. These financial statements do not include any adjustments that might result from the outcome of these uncertainties.

NOTE 3 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

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

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ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

NOTE 3 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

As discussed in Note 8, the Company owns 46% of Pioche and has had voting control for a number of years as a result of a loan which is collateralized by 9% of the outstanding common stock of Pioche. In 1996, the Company concluded that its voting control of Pioche was no longer temporary. Therefore, Pioche has been consolidated in 1996. The financial statements for 1995 and 1994, which account for the investment in Pioche on the equity method, have not been restated.

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

SHORT-TERM INVESTMENT - At December 31, 1996 and 1995, the Company held a United States treasury bill with an original maturity of less than one year. The Company intends to hold this investment to maturity.

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

MINERAL EXPLORATION AND DEVELOPMENT COSTS - All costs related to the acquisition, exploration, and development of mineral deposits are capitalized until such time as (1) the Company commences commercial exploitation of the related mineral deposits at which time the costs will be amortized, (2) the related project is abandoned and the capitalized costs are charged to operations, or (3) when any or all deferred costs are permanently impaired. At December 31, 1996, none of the projects described in Notes 7 and 8 had reached the commercial exploitation stage. No indirect overhead or general and administrative costs have been allocated to any of the projects. In 1996 the Company adopted Statement No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of" and has concluded that there was no impairment at December 31, 1996.

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

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

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

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

STATEMENTS OF CASH FLOWS - On the statements of cash flows, cash includes cash held in the United States. Significant noncash changes in financial position in 1996 include a restructure of debt to include \$445,773 of accrued interest in the loan principal, as well as the issuance of stock and options for services, valued at

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ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

NOTE 3 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

a total of \$1,346,950, which is capitalized as a cost of the Al Masane Project (Note 7). Transactions of this type in 1995 include the write-off of a stockholder receivable to purchase 100,000 shares of common stock at \$1.00 per share and the issuance of 278,000 shares of common stock at \$1.00 per share for the cancellation of \$278,000 of indebtedness (Note 10). Transactions of this type in 1994 include the issuance of 14,000 shares of common stock in exchange for the cancellation of \$14,000 of indebtedness (Note 11).

HEDGING PROGRAM - In July 1994, South Hampton established a hedging program to help decrease the volatility of the price of fuel gas to the refinery. South Hampton purchased several commodity based derivative futures contracts during 1994. Gains and losses related to these contracts are recognized when the contracts expire. The natural gas market suffered severe price declines in the last few months of 1994 and into 1995, which resulted in net recognized losses of \$101,000 in 1995 and \$117,000 in 1994. These losses are included as a cost of refined product sales and processing in the consolidated statements of operations. Since the fuel prices decreased in 1995 and were expected to soften in the next year or two, the hedging program was discontinued in June 1995.

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 occurs. There has been no significant change in the exchange rate for Saudi Riyals to the United States dollar during the period covered by these financial statements. Due to the stability of the Saudi Riyal, the Company feels it has no material exposure to foreign currency risks and does not employ any practices to minimize any such risks. It is anticipated that its products in Saudi Arabia will be sold in US dollars.

GOODWILL - Goodwill acquired in connection with the acquisition of TOCCO in 1987 is being amortized over ten years. The amounts reflected in the balance sheet are net of accumulated amortization of \$2,655,925 and \$2,378,785 at December 31, 1996 and 1995, 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.

STOCK-BASED COMPENSATION - Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation" ("Statement No. 123") is effective for 1996. Statement No. 123 establishes accounting and reporting standards for various stock-based compensation plans. Statement No. 123 encourages the adoption of a fair value based method of accounting for employee stock options, but permits continued application of the accounting method prescribed by Accounting Principles Board Opinion No. 25 ("Opinion 25"), "Accounting for Stock Issued to Employees." Entities that continue to apply the provisions of Opinion 25 are required to make pro forma disclosures of net income and earnings per share as if the fair value based method of accounting had been applied. Refer to Note 11.

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

At December 31, 1996, the Company's financial instruments included cash, cash equivalents, investments, accounts receivable, current obligations, and noncurrent liabilities. The fair values of these items approximate their carrying amounts at December 31, 1996. Accrued liabilities in Saudi Arabia consist primarily of accrued salary and benefits. Payment of these items is contingent on the Company's ability to obtain future financing. As such, a fair value cannot be reasonably estimated.

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

South Hampton, the Company's only revenue producing asset, sells its products primarily to companies in the chemical and plastics industry. Downturns in these industries 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 17%, 25% and 13% of total sales in 1996, 1995 and 1994, respectively.

NOTE 5 - CONTINGENCIES

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

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

South Hampton, is a defendant in two lawsuits in two district courts in Jefferson County, Texas brought on July 21, 1993 and July 18, 1994 by two former employees of the Goodyear Tire & Rubber Company, seeking unspecified actual and punitive damages for certain alleged illness and diseases resulting from alleged exposure to certain chemicals during their employment with Goodyear. One of these lawsuits was settled in March 1997. The cost to the Company, net of expected insurance recovery, is not significant. The outcome of the remaining lawsuit is not expected to have a material effect on the Company's financial position, results of operations or liquidity.

NOTE 5 - CONTINGENCIES - CONTINUED

South Hampton has been spending an increased amount of time and expense on environmental and regulatory functions and compliance. It is South Hampton's policy to accrue costs associated with regulatory compliance when those costs are reasonably determinable. In 1993, while remediating a small spill area, The Texas Natural Resources Conservation Commission ("TNRCC") requested that the refinery drill a well to check for groundwater contamination under the spill area. The well disclosed a pool of hydrocarbons on top of the groundwater under a truck loading rack area. An analysis of the material indicated that the hydrocarbons were produced more than fifteen years ago when the refinery was in the business of processing crude oil. Consulting engineers were hired to help evaluate the size and location of the pool. Monitoring wells were drilled around the perimeter of the refinery property and it was determined that there was no migration of hydrocarbons off the Company's property. Two large pools were located, one under the South Hampton's historic refinery site and one under property which had been purchased from an independent gas producer in 1981. The west plant site had previously been the site of a natural gas processing plant operated by Sinclair, Arco and others. 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 was completed and approved in November 1995. Cleanup expenditures through 1996 were approximately \$153,500, and an additional \$60,000 was accrued at December 31, 1996. The consulting engineers expect approximately 10,000 barrels of recoverable material will be available to South Hampton for use in their refining process, but no accrued income has been recorded due to the uncertainties relating to the recovery process.

In November 1996, South Hampton agreed to a proposed settlement with the TNRCC's Air Permit Section for various alleged violations occurring during the 1991 through 1994 inspections. An agreed fine of \$50,000 will be paid over a period of ten months and an amount adequate to cover the remaining amounts to be paid was accrued as of December 31, 1996. South Hampton vigorously denied many of the allegations in the settlement document, but determined that to further protest the TNRCC's interpretation and application of the rules would ultimately result in higher expenses.

NOTE 5 - CONTINGENCIES - CONTINUED

In addition to the various Environmental Protection Agency and TNRC air, water and solid waste regulations, South Hampton is also subject to the regulations of the U.S. Department of Transportation, the Occupational, Health and Safety Administration and the Texas General Land Office, among others. In response to various regulations from these and other agencies, South Hampton has developed OPA-90 Emergency Response Plans for the pipeline and the refinery, and is in the process of voluntarily adopting the requirements of the OSHA Process Safety Management rules. Approximately \$35,000 and \$80,000 was spent in 1996 and 1995, respectively, on development of this OSHA program. The program is approximately 75% completed and is expected to be completed in 1997 at an additional cost of about \$25,000. Due to the uncertain timing and scope of the additional work, no accruals have been provided.

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, 1996, the past due amount of these rent payments was approximately \$309,000. 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 requirements will not have any effect on the Company's planned operations in Saudi Arabia.

At December 31, 1996, South Hampton had a \$100,000 letter of credit in support of payment for purchases of natural gas used in the refinery from its main supplier.

NOTE 6 - INVENTORIES

Inventories include the following:

<TABLE>

<CAPTION>

	December 31,	
	1996	1995
<S>	<C>	<C>
Refinery feedstock	\$ --	\$ 59,358
Refined products	565,346	371,374
	-----	-----
Total inventories	\$ 565,346	\$ 430,732
	=====	=====

</TABLE>

In 1994, 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, 1996, current cost exceeded LIFO value by approximately \$163,000. At December 31, 1995, current cost approximated LIFO value.

NOTE 7 - MINERAL EXPLORATION AND DEVELOPMENT COSTS IN SAUDI ARABIA

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

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. The Company and NMC also obtained written authority to explore an area of 1,100 square kilometers surrounding Al Masane ("Greater Al Masane"). An exploration license for the Greater Al Masane area has been applied for and verbally approved by the Saudi Arabian government (unaudited).

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 50% of the capital of the Project at such time as the Project proves to be profitable. Subsequently, a formal Mining Lease Agreement assigning the lease solely to the Company was initialed by the Company and the Ministry on October 4, 1992.

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 an \$11 million interest-free loan from the Saudi Arabian government, the proceeds of which were used to fund the Project. The loan was scheduled to be repaid in ten annual installments beginning in 1984. None of the scheduled payments have been made. Pursuant to Article 18 of the Mining Lease Agreement, the Company will repay the loan in accordance with a repayment schedule to be agreed upon with the Saudi Arabian government. As noted below, the mining lease was granted in 1993. However, 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.

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

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

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

On April 26, 1993, the Council of Ministers passed a resolution granting the Company a mining lease for the Al Masane Project, and on May 22, 1993, a Royal Decree was issued by the King. The initial period of the mining lease is 30 years, which can be renewed for another period or periods, not to exceed 20 years. The lease area is 44 square kilometers in size. The lease agreement stipulates that the Company is to pay the Saudi government a surface rental of approximately \$117,000 a year. The Company made the first year's payment in August 1993. All subsequent payments, which amount to \$309,000 at December 31, 1996, are being deferred until a Saudi limited liability company is formed and the mining lease is transferred to it. The Company will own 50% of this new company, which will operate the Project when approval is received for the loan from the Saudi Industrial Development Fund ("SIDF"), which was applied for on September 30, 1995. The lease agreement also stipulates that, after two years of profitable mine operations, a Saudi public stock company will be formed in which the limited liability company will transfer its interest in the Al Masane Project. The Company will own 50% of the stock in the public stock company. The Petroleum and Mineral Organization ("PETROMIN"), a company wholly-owned by the Saudi government, has an option to acquire up to 25% of the stock and the remaining interests not owned by the Company or acquired by PETROMIN are to be put out for public subscription to Saudi citizens.

On March 27, 1995, the board of directors approved a Letter of Agreement between the Company and Carlyle SEAG ("Carlyle"), whereby Carlyle had been retained as the Company's financial advisor in connection with the Al Masane mining project. In March 1996, the agreement with Carlyle was terminated by mutual consent.

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

payment of \$20,000 in cash and the issuance of 300,000 shares of common stock and stock options for 345,000 shares at \$1.00 per share.

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

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

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, and an update prepared in 1996, estimates proven and probable reserves of copper, zinc, silver and gold of 7.2 million tonnes in the Project with the potential to increase these reserves with further exploration. The report projects production of the proven and probable reserves over a twelve-year period. 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 of the new Saudi limited liability company. Revenues were estimated utilizing projected mineral prices from a third party pricing expert. The report projected positive net cash flows to the Company of \$37 million over the life of the Project. According to the provisions of Article 46 of the Saudi Mining Code, no taxes will be payable to the Saudi government during the first stage of operations on a mining lease, which is the period of five years starting from the earlier of (a) the date of the first sale of products or (b) the beginning of the fourth year since the issue of the lease.

Deferred development costs of the Al Masane Project at December 31, 1996, 1995 and 1994, and the changes in these amounts for each of the three years then ended are detailed below:

<TABLE>
<CAPTION>

	Balance at December 31, 1996	Activity for 1996	Balance at December 31, 1995	Activity for 1995	Balance at December 31, 1994	Activity for 1994
<S>	<C>	<C>	<C>	<C>	<C>	<C>
Property and equipment:						
Mining equipment	\$ 2,160,206		\$ 2,160,206		\$ 2,160,206	
Construction costs	3,140,493		3,140,493		3,140,493	
Total	5,300,699		5,300,699		5,300,699	
Other costs:						
Labor, consulting services and project administration costs	18,582,773	\$ 1,942,586	16,640,187	\$ 616,912	16,023,275	\$ 237,908
Materials and maintenance	6,167,924	914	6,167,010	5,326	6,161,684	683
Feasibility study	2,831,442	41,455	2,789,987	163,513	2,626,474	505,118
Total	27,582,139	1,984,955	25,597,184	785,751	24,811,433	743,709
	\$32,882,838	\$ 1,984,955	\$30,897,883	\$ 785,751	\$30,112,132	\$ 743,709

</TABLE>

The deferred development costs of the "Other interests in Saudi Arabia", in the total amount of approximately \$2.4 million, consist of approximately \$1.5 million associated with the Greater Al Masane area and the balance of approximately \$900,000 is associated primarily with the Wadi Qatan and Jebel Harr areas. These costs have not changed since 1993. In the event an exploration license for these areas is not granted, the entire amount of deferred development costs relating thereto would be written off.

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

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

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. Cash in Saudi Arabia includes time deposits of \$0 and \$300,735 at December 31, 1996 and 1995, respectively.

NOTE 8 - MINERAL PROPERTIES IN THE UNITED STATES

The Company has voting rights of approximately 55% and directly owns approximately 46% of the outstanding common stock of Pioche. During 1988, 634,223 shares of Pioche stock were deemed acquired through in-substance foreclosure on a \$114,537 note due from the issuer's estate. The original date of the note was May 31, 1985, and the note was due on May 31, 1995; however, management of the Company extended the due date to December 31, 1998 to allow the estate the opportunity to pay off the note. Until the note is paid, the Company has the voting rights to these shares. At this time, it is not possible to determine whether the issuer's estate will be able to repay the note when due. If the note is not repaid, the Company could take ownership of the shares. At December 31, 1996, the Company determined the loan was not likely to be repaid, and has consolidated the accounts of Pioche in the accompanying financial statements for 1996. Previously, the investment in Pioche was accounted for on the equity method. The consolidation of Pioche increased total assets at December 31, 1996 by approximately \$1,200,000 and had no effect on the net loss reported for 1996.

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. Due to the lack of capital, the properties held by Pioche have not been commercially operated for approximately 35 years. During 1994, Pioche attempted to drill a core hole on this property. The core hole was intended to go down to 1,500 feet but encountered formation problems at 700 feet and further drilling had to be abandoned. A new site will be selected and management expects a second core hole to be drilled when financing becomes available. In late 1996, Pioche was extended a proposal from a prominent mining company for the lease of its mining claims. This proposal is currently being negotiated.

In August 1993, Pioche entered into a lease of the Wide Awake mine property. This agreement stipulated 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 (to December 31, 1995). In August 1995, it was agreed by all parties concerned that the lease be extended for one year to December 31, 1996, under the same terms. No significant work took place on the property and no royalties were earned. The lease was not extended and it has expired. In 1995, the Company received an extension of its option to buy 720,000 shares (approximately 10% of the outstanding shares) of Pioche common stock at \$0.20 per share. The option expires on June 1, 1997.

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

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

<TABLE>
<CAPTION>

	1996	1995
	-----	-----
<S>	<C>	<C>
Notes payable:		
Revolving bank note. See (A)	\$ --	\$ 2,222,911
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
Unsecured note to a Saudi investor. See (D)	13,280	13,280
Unsecured note to a Saudi investor. See (E)	350,000	350,000
Other	12,500	--
	-----	-----
Total	\$ 11,375,780	\$ 15,086,191
	=====	=====
Long-term debt:		
Revolving bank note. See (A)	\$ 1,890,000	\$ --
Unsecured note to a Saudi company. See (C)	1,945,773	--
Unsecured notes to foreign investors. See (F)	598,000	598,000
Bank note. See (G)	103,068	188,624
	-----	-----

Total	4,536,841	786,624
Less current portion	(992,729)	(78,090)
	-----	-----
Total	\$ 3,544,112	\$ 708,534
	=====	=====
Long-term obligations:		
Noninterest-bearing note to a supplier and customer for capital improvements. See (H)	\$ 128,683	\$ 128,683
Deferred compensation contracts. See (I)	57,230	77,477
	-----	-----
Total	185,913	206,160
Less current portion	(150,904)	(20,285)
	-----	-----
Total	\$ 35,009	\$ 185,875
	=====	=====

</TABLE>

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

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ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

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

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

- (B) The Company has an interest-free loan of \$11,000,000 from the Saudi Arabia Ministry of Finance and National Economy, the proceeds of which were used to finance the development phase of the Al Masane Project. The loan was repayable in ten equal annual installments of \$1,100,000, with the initial installment payable on December 31, 1984. None of the ten scheduled payments have been made. Pursuant to the mining lease agreement covering the Al Masane Project, the Company will repay the loan in accordance with a repayment schedule to be agreed upon with the Saudi Arabian government. 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 note is now owed by South Hampton to Saudi Fal. On October 15, 1996, South Hampton and Saudi Fal agreed to restructure the loan terms, whereby the accrued interest to date of \$445,773 was added to principal, the interest rate was set at prime plus

1%, and the maturity date is now December 31, 1998. This new note has a second lien position behind the bank's position as discussed in (A) above and is convertible into 1,945,773 shares of common stock.

(D) Represents a noninterest demand loan payable to a Saudi investor. In September 1995, this investor loaned the Company an additional \$123,000. The loan agreement granted an option to convert the loan into shares of the Company's common stock at \$1 per share. Also in September 1995, the investor exercised this option and converted the \$123,000 loan into 123,000 shares of the Company's common stock (see Note 11). In December 1995, the investor agreed to exchange \$155,000 of his debt balance for 155,000 shares of the Company's common stock.

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

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

- (E) Represents an unsecured, noninterest bearing advance made by a Saudi investor in 1984 to the Al Masane Project.
- (F) Represents loans payable to a stockholder of the Company for \$245,000, the Company's president for \$53,000 and a relative of the Company's president and stockholder for \$300,000. Each loan is due in 1997, with interest payable at the LIBOR rate plus 2% at maturity. Each loan provides for an option to convert the loan amount to shares of the Company's common stock at \$1.00 per share anytime within five years from the date of the loan. See Note 11 for a discussion of the related options.
- (G) 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, 10.25% from February 1, 1996 to February 1, 1997, and 9.75% thereafter.
- (H) 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. As of December 31, 1996, these criteria have been met.
- (I) In connection with the acquisition of TOCCO, deferred compensation contracts between TOCCO and a certain former employee and one current employee were restructured, reducing the gross payments due under the original contracts. Default on payments due under the restructured agreements would invalidate the negotiated settlement amounts resulting in TOCCO being liable for the amounts due under the original contracts. TOCCO has complied with the terms of these contracts through 1996. However, if TOCCO were to default on these contracts, it would be liable for an additional amount of \$448,300. The recorded liability at December 31, 1996 and 1995 has been determined utilizing a discount rate of 8.0%.

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

<TABLE>		
<S>	<C>	<C>
	1997	\$1,143,633
	1998	2,245,773
	1999	1,333,348

	Total	\$4,722,754
		=====
</TABLE>		

Interest of \$186,190, \$244,828 and \$275,561 was paid in 1996, 1995 and 1994, respectively.

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

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

In May 1994, South Hampton settled a note payable and accrued interest payable to a vendor for \$175,000 cash. An extraordinary gain of \$578,150, for which there was no tax effect after application of operating loss carryforwards was recorded, representing the amounts forgiven.

NOTE 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. In June 1992, Mr. Bomer withdrew from the partnership and the feedstock agreement 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 had a liability to STTC for the cost of the 453,600 gallons of capacity of the pipeline. This amount was \$215,460 at December 31, 1994. Also in connection with this agreement, South Hampton paid a one-half cent per gallon fee to STTC on each gallon of feedstock transported through the pipeline. The agreement was operating on a month to month basis and was terminated in August 1995. The fees paid by South Hampton to STTC pursuant to this agreement were \$76,080 and \$103,212 in 1995 and 1994, respectively.

South Hampton leases vehicles and equipment for use in operations for approximately \$29,000 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 related to this agreement of approximately \$349,000, \$316,000 and \$341,000 in 1996, 1995 and 1994, respectively.

The Company incurred rental expenses for office space and certain vehicles and equipment of approximately \$367,000, \$302,000 and \$302,000 in 1996, 1995 and 1994, respectively.

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, 1996 of \$310,926 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 included in other assets. As described in Note 9, the leased building is pledged as collateral for a note payable. If the lessee exercises its option to purchase the building, the proceeds will be used to pay down the note payable. Miscellaneous income includes approximately \$102,000 in 1996, 1995 and 1994 of rental income pursuant to this lease.

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

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

NOTE 11 - COMMON STOCK AND STOCK OPTIONS

At December 31, 1996, Saudi Arabian investors owned approximately 63% of the Company's outstanding common stock.

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

Notes receivable from stockholders for the purchase of common stock of \$126,000 at December 31, 1996 and 1995 represents a note from a director and officer which matures on December 31, 1998. Notes receivable from stockholders are classified as a reduction of stockholders' equity.

At December 31, 1996, a note payable was convertible into 1,945,773 shares of common stock (See Note 9).

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. 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.

To enhance the Company's ability to obtain and retain qualified directors, it instituted the 1987 Non-Employee Director Stock Option Plan (the "Non-Employee Director Plan") which provides for each non-employee director to receive an option for 10,000 shares of common stock upon election to the board of directors with the exercise price equal to the fair market value of the stock at the date of grant. The number of shares reserved for issuance under this plan is 100,000. The Non-Employee Director Plan was instituted in 1987 for a duration of ten years and in 1997 it will expire. Then, a new plan may be instituted at a later date. At December 31, 1996, 40,000 shares had been granted, 20,000 had been forfeited and none had been exercised.

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

NOTE 11 - COMMON STOCK AND STOCK OPTIONS - CONTINUED

A summary of stock option transactions under the Employee Plan and Non-Employee Director Plan is as follows:

<S>	<C>
Outstanding December 31, 1993	160,000
Granted (\$1.75 per share)	75,000
Expired	(20,000)

Outstanding at December 31, 1994, 1995 and 1996	215,000
	=====

</TABLE>

Under the above plans, 207,000 options were exercisable at prices ranging from \$1.38 to \$3.75 per share and 385,000 shares were reserved for grant at December 31, 1996. The options for the Employee Plan vest at such times and in such amounts as is determined by the Compensation Committee of the board of directors at the date of grant. The options for the Non-Employee Director Plan vest in cumulative annual installments of 20% beginning one year from the date of grant. The options for both plans are exercisable for a period of ten years.

In 1994, a director and officer of the Company exercised an option to purchase 14,000 shares of common stock at \$1.00 per share in exchange for cancellation of \$14,000 of unpaid compensation.

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

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

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

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

NOTE 11 - COMMON STOCK AND STOCK OPTIONS - CONTINUED

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

For the options to purchase 668,000 shares of stock granted to investors during 1995, the Company recognized an expense of \$ 76,500, which is included in general and administrative expense in the Company's results of operations for the year ended December 31, 1995. This expense is based on the fair value of the options as of the grant date. For the options to purchase 400,000 shares of stock granted to the Company's president in 1995, the Company recorded compensation expense in the amount of \$74,900, which is included in general and administrative expense in the Company's results of operations for the year ended December 31, 1995. This expense is based on the difference between the market price of the Company's stock as of the grant date and the price of the option.

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

<TABLE> <S>	<C>
Outstanding December 31, 1993	14,000
Exercised	(14,000)

Outstanding at December 31, 1994	--
Granted (\$1.00 per share)	1,121,000
Exercised	(123,000)

Outstanding at December 31, 1995	998,000
Granted (\$1.00 per share)	345,000

Outstanding at December 31, 1996	1,343,000
	=====

</TABLE>

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

The Company has adopted only the disclosure provisions of Statement No. 123, as discussed in Note 3. Therefore, compensation expense for stock options granted to employees is measured as the excess, if any, of the quoted market price of the Company's stock at the date of grant over the amount an employee must pay to acquire the stock. If the Company recognized compensation expense based upon the fair value at the grant date for options granted to employees in 1995 (none were granted in 1996), the Company's 1995 and 1996 net loss and loss per share would be increased to the pro forma amounts indicated as follows:

<TABLE> <CAPTION>	1996	1995
<S>	<C>	<C>
	-----	-----
Net loss		
As reported	\$ (390,896)	\$ (369,232)
Pro forma	(390,896)	\$ (726,332)
Loss per common share		
As reported	\$ (.02)	\$ (.02)
Pro forma	\$ (.02)	\$ (.04)

</TABLE>

NOTE 11 - COMMON STOCK AND STOCK OPTIONS - CONTINUED

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

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

Additional information with respect to all options outstanding at December 31, 1996, and changes for the three years then ended was as follows:

<TABLE>
<CAPTION>

	1994	
	Shares	Weighted average exercise price
<S>	<C>	<C>
Outstanding at beginning of year	174,000	\$ 1.74
Granted	75,000	1.75
Forfeited	(20,000)	1.38
Exercised	(14,000)	1.00
	-----	-----
Outstanding at end of year	215,000	\$ 1.83
	=====	=====
Options exercisable at December 31, 1994	161,500	\$ 1.74
	=====	=====

</TABLE>

<TABLE>
<CAPTION>

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

</TABLE>

<TABLE>
<CAPTION>

	1996	
	Shares	Weighted average exercise price
<S>	<C>	<C>
Outstanding at beginning of year	1,213,000	\$ 1.15
Granted	345,000	1.00
	-----	-----
Outstanding at end of year	1,558,000	\$ 1.11
	=====	=====
Options exercisable at December 31, 1996	1,550,000	\$ 1.10
	=====	=====
Weighted average fair value per share of options granted during 1996		\$ 2.31
		=====

</TABLE>

NOTE 11 - COMMON STOCK AND STOCK OPTIONS - CONTINUED

Information about stock options outstanding at December 31, 1996 is summarized as follows:

<TABLE>
<CAPTION>

	Options outstanding		
Range of exercise prices	Number outstanding	Weighted average remaining contractual life	Weighted average exercise price
<S>	<C>	<C>	<C>
\$0 to 1	1,343,000	8.1 years	\$1.00

\$1 to 2	175,000	8.3 years	1.53
\$2 to \$3.75	40,000	4.3 years	3.10

	1,558,000		\$1.11
	=====		=====

</TABLE>

<TABLE>

<CAPTION>

Range of exercise prices	Options exercisable	
	Number exercisable	Weighted average exercise price
<S>	<C>	<C>
\$0 to 1	1,343,000	\$1.00
\$1 to 2	175,000	1.53
\$2 to \$3.75	32,000	3.04

	1,550,000	\$1.10
	=====	=====

</TABLE>

NOTE 12 - INCOME TAXES

The income (loss) before income taxes and extraordinary item was (\$390,896), (\$369,232), and \$2,314,129 for the years ended December 31, 1996, 1995 and 1994, respectively.

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

<TABLE>

<CAPTION>

	1996	1995	1994
<S>	<C>	<C>	<C>
Federal			
Current	\$ --	\$ --	\$522,938
Deferred	--	--	--
Utilization of operating loss carryover	--	--	(482,965)
	-----	-----	-----
Provision for income taxes	\$ --	\$ --	\$ 39,973
	=====	=====	=====

</TABLE>

NOTE 12 - INCOME TAXES - CONTINUED

Income tax expense (benefit) for the years ended December 31, 1996, 1995 and 1994 differs from the amount computed by applying the applicable U.S. corporate income tax rate of 34% to net income (loss) before income taxes. The reasons for this difference are as follows:

<TABLE>

<CAPTION>

	1996	1995	1994
<S>	<C>	<C>	<C>
Income taxes at U.S. statutory rate	\$ (132,905)	\$ (125,539)	\$ 786,804
Goodwill amortization	94,228	95,303	95,303
Liability reserves	--	--	(392,700)
Net operating losses	37,924	25,731	(482,965)
Alternative minimum tax	--	--	39,973
Other items	753	4,505	(6,442)
	-----	-----	-----
Total tax expense	\$ --	\$ --	\$ 39,973
	=====	=====	=====

</TABLE>

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities for 1996, 1995 and 1994 were as follows:

<TABLE>

<CAPTION>

	December 31,		
	1996	1995	1994
<S>	<C>	<C>	<C>

Deferred tax liabilities:			
Refinery plant, pipeline and equipment	\$ (287,845)	\$ (368,385)	\$ (379,668)
Deferred tax assets:			
Accounts receivable	57,284	49,544	44,070
Mineral interests	196,446	196,446	196,446
Accrued liabilities	32,300	--	--
Net operating loss carryovers (NOLs)	11,333,611	11,274,638	9,277,552
Tax credit carryovers	221,322	651,504	650,907
	-----	-----	-----
Gross deferred tax assets	11,840,963	12,172,132	10,168,975
Valuation allowance	(11,553,118)	(11,803,747)	(9,789,307)
	-----	-----	-----
Net deferred tax assets	287,845	368,385	379,668
	-----	-----	-----
Net deferred taxes	\$ --	\$ --	\$ --
	=====	=====	=====

</TABLE>

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ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

NOTE 12 - INCOME TAXES - CONTINUED

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

At December 31, 1996, the Company had approximately \$33,335,000 of net operating loss carryforwards and approximately \$180,000 of general business credit carryforwards. These carryforwards expire in 1997 through 2010. In addition, the Company has minimum tax credit carryforwards of approximately \$40,000 that may be carried over indefinitely. Approximately \$1,700,000 of the net operating loss carryforwards and \$180,000 of the general business credit carryforwards are limited to the net income of TOCCO. Approximately \$5,900,000 of the net operating loss carryforwards are limited to the net income of the Coal Company.

The Company has no Saudi Arabian tax liability.

NOTE 13 - SEGMENT INFORMATION

The Company has operations in two industry segments and geographic regions. Its refinery operations represent the significant portion of its current operating results and are exclusively in the United States, whereas its mining operations, conducted mainly in Saudi Arabia, mostly relate to costs which have been deferred during the development phase of these operations. The only mining operations conducted in the United States relate to the Company's investment in Pioche 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.

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

For 1996, 1995 and 1994, essentially all activity on the Company's consolidated statement of operations relates to the refinery. The 1996, 1995 and 1994 results include \$33,944, \$54,063 and \$74,580, respectively, of unallocated costs recorded in general and administrative expenses related to the Saudi Arabian operations. The 1996 and 1995 results include immaterial amounts of interest expense related to notes payable entered into in 1995 that relate to the Saudi Arabian mining operations. All items included in the Company's consolidated balance sheet related to the Saudi Arabian operations are specifically identified on the face of the consolidated balance sheet with the exception of notes payable which have been identified in Note 9.

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

NOTE 14 - RELATED PARTY TRANSACTIONS

The Company shares office facilities and certain expenses with companies owned by the chairman of the Company. At December 31, 1996 and 1995, these companies did not owe any amounts to the Company.

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

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

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ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

ASSETS

<TABLE>
 <CAPTION>

	DECEMBER 31,	
	1996	1995
<S>	<C>	<C>
Current Assets		
Cash and cash equivalents in United States.....	\$ 209,251	\$ 302,039
Short-term investments.....	298,726	294,610
Accounts receivable (net of allowance for doubtful accounts of \$168,484 in 1996 and \$145,709 in 1995).....	2,643,691	1,791,821
Inventories.....	565,346	430,732
	-----	-----
Total current assets.....	3,717,014	2,819,202
Cash in Saudi Arabia.....	176,039	396,809
Refinery Plant, Pipeline and Equipment -- at Cost.....	5,758,852	5,563,776
Less Accumulated Depreciation.....	2,911,823	2,557,454
Refinery Plant, Pipeline and Equipment, Net.....	2,847,029	3,006,322
Al Masane Project.....	32,882,838	30,897,883
Other Interests in Saudi Arabia.....	2,431,248	2,431,248
Mineral Properties in the United States.....	1,418,615	--
Investment in and Advances to Pioche-Ely Valley Mines, Inc.....	--	239,032
Goodwill.....	117,598	397,902
Other Assets.....	505,566	617,019
	-----	-----
Total Assets.....	\$ 44,095,947	\$ 40,805,417
	=====	=====

LIABILITIES AND STOCKHOLDERS' EQUITY

Current Liabilities		
Accounts payable.....	\$ 1,408,677	\$ 674,641
Accrued liabilities.....	520,445	617,995
Accrued liabilities in Saudi Arabia.....	1,174,229	1,011,980
Notes payable.....	11,375,780	15,086,191
Current portion of long-term debt.....	992,729	78,090
Current portion of long-term obligations.....	150,904	20,285
	-----	-----
Total current liabilities.....	15,622,764	17,489,182
Long-Term Debt.....	3,544,112	708,534
Long-Term Obligations.....	35,009	185,875
Accrued Liabilities in Saudi Arabia.....	714,143	636,047
Deferred Revenue.....	129,685	145,189
Commitments and Contingencies.....	--	--
Minority Interest in Consolidated Subsidiary.....	1,003,590	--
Stockholders' Equity		
Common stock, authorized 40,000,000 shares of \$.10 par value: issued and outstanding, 20,956,494 shares in 1996 and 20,206,494 shares in 1995.....	2,095,649	2,020,649
Additional paid-in capital.....	34,932,700	33,210,750
Receivables from stockholders.....	(126,000)	(126,000)
Accumulated deficit.....	(13,855,705)	(13,464,809)
	-----	-----
Total stockholders' equity.....	23,046,644	21,640,590
	-----	-----
Total Liabilities and Stockholders' Equity.....	\$ 44,095,947	\$ 40,805,417
	=====	=====

</TABLE>

The accompanying notes are an integral part of these statements.

ARABIAN SHIELD DEVELOPMENT COMPANY AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS
FOR THE THREE YEARS ENDED DECEMBER 31, 1996<TABLE>
<CAPTION>

	1996	1995	1994
	-----	-----	-----
<S>	<C>	<C>	<C>
Revenues			
Refined product sales.....	\$21,367,438	\$17,741,862	\$17,564,226
Processing fees.....	646,848	616,796	200,757
	-----	-----	-----
	22,014,286	18,358,658	17,764,983
Operating costs and expenses			
Cost of refined product sales and processing.....	19,357,737	15,575,054	13,750,750
General and administrative.....	2,284,422	2,372,683	2,036,470
Depreciation and amortization.....	693,251	677,157	647,137
Litigation.....	--	--	(975,000)
	-----	-----	-----
	22,335,410	18,624,894	15,459,357
Operating income (loss).....	(321,124)	(266,236)	2,305,626
Other income (expense) Interest income.....	25,310	33,395	56,491
Interest expense.....	(336,979)	(369,546)	(347,364)
Minority interest.....	13,072	--	--
Equity in losses of affiliate.....	--	(24,112)	(114,460)
Miscellaneous income.....	228,825	257,267	443,836
	-----	-----	-----
Income (loss) before income taxes and extraordinary item.....	(390,896)	(369,232)	2,314,129
Income tax expense.....	--	--	(39,973)
	-----	-----	-----
Income (loss) before extraordinary item.....	(390,896)	(369,232)	2,274,156
Extraordinary item.....	--	--	578,150
	-----	-----	-----
Net income (loss).....	\$ (390,896)	\$ (369,232)	\$ 2,852,306
	=====	=====	=====
Per common share Income (loss) before extraordinary item.....	\$ (0.02)	\$ (0.02)	\$ 0.11
Extraordinary item.....	--	--	0.03
	-----	-----	-----
Net income (loss).....	\$ (0.02)	\$ (0.02)	\$ 0.14
	=====	=====	=====
Weighted average number of common shares outstanding.....	20,286,208	20,030,434	20,027,881
	=====	=====	=====

</TABLE>

The accompanying notes are an integral part of these statements.

<TABLE> <S> <C>

<ARTICLE> 5

<LEGEND>

THIS SCHEDULE CONTAINS SUMMARY FINANCIAL INFORMATION EXTRACTED FROM FORM 10-K AND IS QUALIFIED IN ITS ENTIRETY BY REFERENCE TO SUCH FINANCIAL STATEMENTS.

</LEGEND>

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