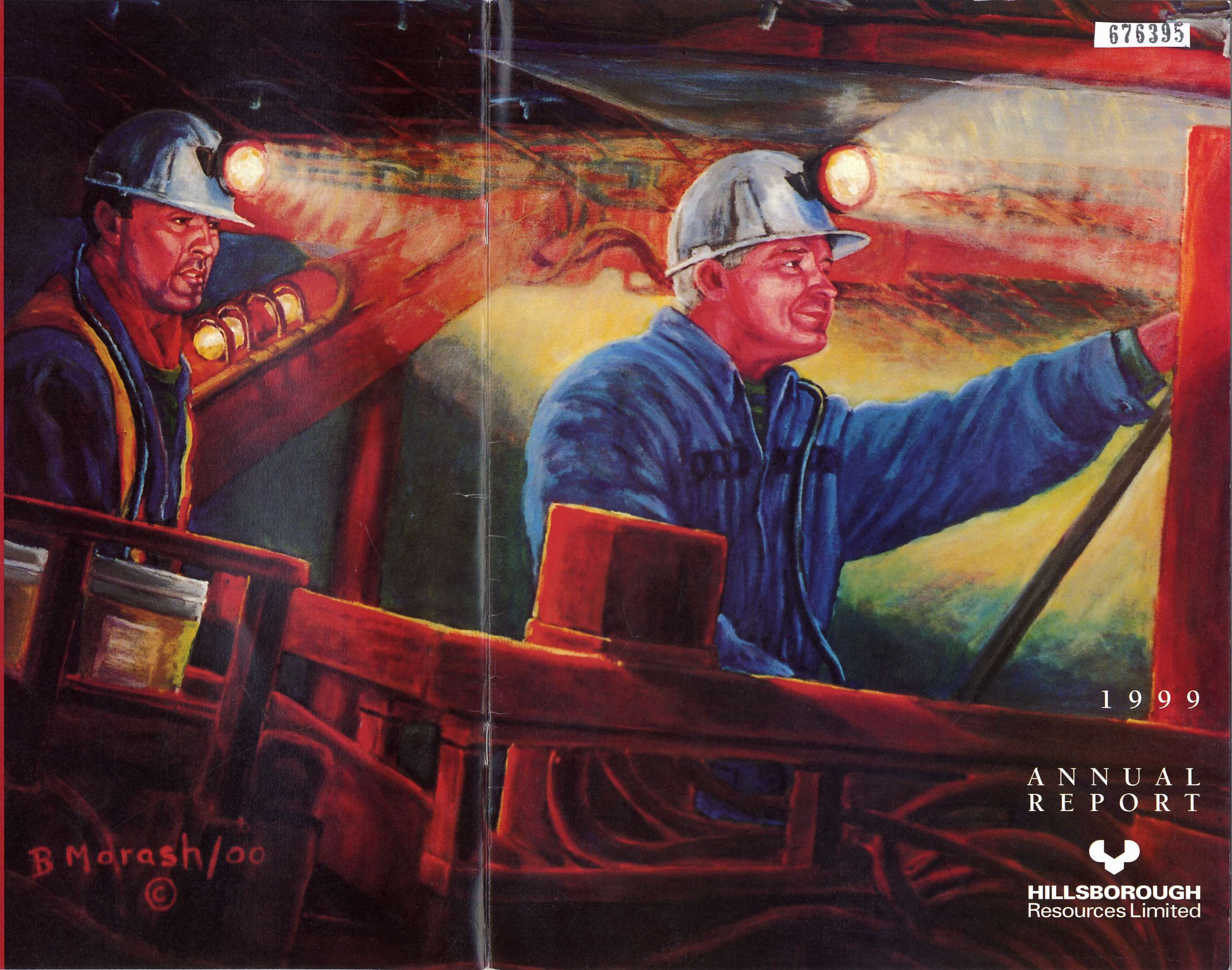
HILLSBOROUGH
Resources Limited



1999

ANNUAL REPORT

HILLSBOROUGH
Resources Limited

HILLSBOROUGH RESOURCES LIMITED

1999 ANNUAL REPORT

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HILLSBOROUGH RESOURCES LIMITED

PRESIDENT'S REPORT TO THE SHAREHOLDERS

Financial and Operating Results

For the years ended December 31

	1999	1998	1997
Consolidated net income (loss)	$(26.9) million	$(9.6) million	$4.3 million
Earnings (loss) per share	$(1.55)	$(0.54)	$0.25
Income from operations	$1.7 million	$0.4 million	$6.1 million
Sales revenue	$14.9 million	$29.7 million	$44.5 million
Clean coal production-tonnes	362,000	707,000	1,066,000
Clean coal sales-tonnes	354,000	684,000	1,040,000
Net coal sales price/tonne	$42.01	$43.42	$42.79

In my last report to shareholders I expressed some optimism for a return to profitability for your company in 1999. Financing initiatives with our bankers and the Provincial Government came close to fruition but collapsed due to unanticipated security requirements. These initiatives would have provided the working capital that had been eroded by the cash losses resulting from very weak Japanese coal contract prices experienced during 1998. As a direct result of these two actions, Quinsam Coal Corporation was forced to seek protection from its creditors under the *Companies' Creditors Arrangement Act (CCAA)* on May 14, 1999. Hillsborough followed suit on May 20, 1999.

Without a bank line of credit, Quinsam had to tailor its operations to a level that could be financed by its parent's cash resources. Production was reduced to cover only that coal required to honour Quinsam's domestic customer contracts, approximately 240,000 tonnes per annum. Further layoffs were required to accommodate this reduction in tonnage, and Quinsam is currently operating with thirty people.

In March 2000 the company was successful in selling 2,000,000 shares of its holdings in Canabrava Diamond Corporation for a net realization of $3.45 million. This sale has provided substantial assistance in formulating a plan of arrangement to bring both Hillsborough and Quinsam out of CCAA.

Operations

During the period January 1999 until mid-May 1999, the Quinsam mine operated at an annualized rate of 600,000 tonnes. Shortly after seeking protection, the mine was put onto a care and maintenance mode while legal arrangements were made for Quinsam to obtain financing from Hillsborough to allow a resumption of operations.

In mid-June 1999, the mine recommenced operation at a reduced production level of 240,000 per annum. This level was sufficient to generate positive cash flow of approximately $1.5 million on an annualized basis, but the heavy legal and other costs of CCAA resulted in only a breakeven cash outcome for the balance of the year.

I am pleased to report that productivity per man-hour is at the highest level ever seen at Quinsam, and my congratulations go out to all concerned.

Safety

It is my firm belief that sustained high productivity can only be achieved in a safe working environment. While attitude of the workforce is a significant contributor, it is incumbent on management to take the initiative and promote safety above all else. Our safety record at Quinsam was not satisfactory. In 1998 the mine experienced 44 lost time accidents (LTAs). Steps were taken to significantly bolster safety training and a group and individual award initiatives were introduced effective January 1999. This action has paid off. In 1999 the mine had only one LTA, and for the first time ever, won the coveted British Columbia Small Underground Mine safety award for 1999.

On May 7th, 2000, the mine enjoyed its 365th day without an accident.

Capital Expenditures

It was our intention to acquire two major items of mining equipment in 1999, a Fletcher roof-bolter and a rebuilt Joy 12CM12 continuous miner. The roof-bolter was delivered on time and within budget, and I am pleased to report that it has proved to be an excellent acquisition. Its cycle time is significantly higher than any of the bolters we have at Quinsam, leading to much improved productivity in our development panels. I should also add that this bolter has very much enhanced safety features, backing up our position that "Safety is Job #1".

Unfortunately, Quinsam's financial problems crystallized just days before the scheduled shipping of the continuous miner, and we were forced to put this item on hold. This piece of equipment remains a top acquisition priority when our financial position improves.

A new vent raise was completed in April 1999, providing much-needed ventilation to our new development areas.

Environmental

Despite very much reduced staffing levels, environmental monitoring of our various lakes and ponds continued at regular intervals. Some increases in sulphate levels have been recorded in No-Name Lake and, in conjunction with the Environment Ministry, a series of ground-water bore-holes has been sunk to determine the source.

At our Middle-Point coal terminal, engineering was completed during the year to determine the best means for Quinsam to lower its particulate run-off as part of a plan targeting full permitting of the site by September 2000. Full permitting will result in a lower user fee payable to the British Columbia Transport Finance Authority, who originally financed the terminal.

Financing

Since mid-June, 1999, Quinsam's operations have been financed entirely by surplus cash within its parent, Hillsborough Resources. Advances have been made on the same terms and conditions that had been previously in force with Quinsam's commercial bank, (ie fully secured and margined against inventory and receivables). With an upper advance limit set at $2.4 million, the mine was unable to build inventories to access offshore contracts, and focussed instead solely on its domestic contracts.

As a secured creditor condition to the CCAA application Quinsam arranged for an appraisal of the mine in June 1999. As a result of this valuation, which did not include coal reserves, and in consultation with our auditors, management has deemed it prudent to write down a substantial part of Quinsam's assets. The effect of this can be seen in the financial statements accompanying this report.

Discussions have been held with a major Canadian Chartered bank to take over the credit line presently provided internally. We have had a positive response, but any further action will require Quinsam's coming out of CCAA.

Methane Gas

Between Quinsam and its sister company, T'Sable River Coal Corporation, your company controls approximately 117,000 acres of coal beds on the eastern seaboard of Vancouver Island. Based on historical data, this holding may contain commercially viable amounts of methane gas. Vancouver Island is energy poor; currently only 25% of the energy consumed on the island is actually produced on the Island. A new energy source in the form of methane gas could be expected to be of great interest to companies like BC Hydro and Centra Gas, whose supplies of gas for both domestic consumption and electrical generation presently comes from the mainland.

The potential has cultivated interest from several oil and gas companies, and over the last twelve months two companies inspected the properties and reviewed the extensive core hole and seismic work we did on the T'Sable River property. One of these companies was McMurry Oil, a gas producer based in Casper, Wyoming. Another was Vassilopoulos and Williamson, (VW) a partnership based in Midland, Texas.

An agreement was reached with VW in August 1999 for the payment of a substantial up-front advance on royalties in return for an assignment of drilling and extraction rights in the Quinsam/T'Sable River area. VW needed financing for a major project of this size, and approached a New York company, Vulcan Capital Management. After visiting the mine, looking over the properties and examining our seismic work, negotiations commenced with a view to Vulcan taking control of Hillsborough by means of an open market offer for sufficient shares to give them 51% of the company. However, when finally received, Vulcan's offer called for it to acquire 95% of your company. The Vulcan proposal would have required approval by the Toronto Stock Exchange ("TSE").

Against the eventuality that the Vulcan offer would not receive the necessary approvals, we accepted a back-up proposal from McMurry. McMurry's proposal provided the funds necessary to solve Quinsam's financial situation, and did not require any dilution of shareholder interest. In addition it provided for royalties to Hillsborough on the methane produced. The McMurry proposal is subject to a number of conditions and is not finalized.

Vulcan have objected to the McMurry proposal, but have still not authorized us to issue a proxy circular to determine our shareholders' views on their proposal. Preliminary indications are that TSE approval would not be forthcoming

The Future

I believe that our decision to focus Quinsam's efforts on the domestic market was the right one, especially in the light of even further drops in the Australian Benchmark price for coal recently announced in Japan. Our marketing efforts have begun to pay off, with the first shipment of

10,000 tons to a new domestic customer occurring earlier this month. Other opportunities are available, and we are confident that we will procure further additional contracts later this year.

I recently announced extensions to two of our major domestic fixed price contracts. These extensions remove price risk from the Quinsam equation, and as long as we can continue to control costs as well as we have over the last twelve months, I am confident that your company can produce positive earnings in the years to come.

The closure of the pulp mill at Gold River provides a potential opportunity for us to generate electricity using Quinsam coal. Preliminary discussions have taken place with BC Hydro for an off-take agreement, as well as with a major private utility company to joint venture the project and provide technical and operating expertise.

Conclusion

We are finally starting to see the light at the end of what has been a long and dark tunnel. The coal mining operations have been generating positive cash contributions. The sale of the Canabrava shares along with on-going negotiations with McMurry Oil for a five year term loan would if completed, provide the funds to repay secured creditors. It is reasonable to anticipate that a plan of arrangement will now be able to be submitted that will allow both Hillsborough and Quinsam to emerge from CCAA in the near future.

My thanks go to all the Quinsam and Hillsborough team for a great result under very difficult conditions.

Respectfully submitted,

David J. Slater
President & CEO

HILLSBOROUGH RESOURCES LIMITED

Management Discussion and Analysis

1999 Overview

The 1999 operations of Hillsborough's subsidiary coal mining company, Quinsam Coal Corporation, can most easily by viewed in two parts: pre *Companies' Creditors Arrangement Act (CCAA)* and post *CCAA*. Prior to seeking protection from creditors in May 1999, Quinsam was operating with a workforce of approximately 120 men, producing 500,000 tonnes of coal on an annualized basis for fixed price domestic contracts and certain contracts with Japanese customers. The withdrawal of its bank line of credit precipitated the filing for CCAA. In mid-June 1999, Hillsborough took over the position of the TD Bank, providing secured, demand advances, margined against inventory and receivables. The level of advance permitted by the courts only allowed for limited ongoing production (at a level of 240,000 tonnes per annum), and accordingly plans were made to further shrink Quinsam's operations. Regrettably this resulted in still further layoffs, reducing the work force to 30 people.

The remaining workforce responded to the challenges presented and productivity increased substantially. This was due to an improved equipment maintenance plan that resulted in less down time and in part to an increase in motivation of the workforce. Evidence of this was the significant improvement in the mine's safety record, with only one lost time accident being recorded in 1999.

Further cost reductions were achieved by selective pruning of unneeded overhead. As a result of rigid cost controls and a better price realization in the post-*CCAA* period, income from coal operations improved considerably, from $350,000 in 1998 to $1.7 million in 1999.

During the year the company looked into the possibility of exploration for coal bed methane on the Quinsam property and the T'Sable River coal lands held under option. The company is continuing to investigate the commercial production of coal bed methane.

Watson Lake Operation (Canadian Mine Development)

During the year all of the Watson Lake assets were sold. The exception was a small parcel of land currently leased to Cominco Limited. Cominco has since entered into an agreement with Hillsborough to purchase the land, and a closing is expected by mid-2000. Profit from the disposition of these assets will aggregate in excess of $500,000.

Ongoing Projects

There are two projects which commenced in 1999 and still in progress at year end:

- With the assistance of Stothert Engineering, a pre-feasibility study was undertaken to determine the economic viability of the "energy island" assets at Bowater's now-closed pulp-mill at Gold River, BC. The energy island consists of a 25 megawatt (MW) power boiler designed to burn hog-fuel, but which could be converted to burning coal fairly easily. In addition, there is a black liquor recovery boiler which we believe can be converted to a coal-burning power boiler, and with the addition of two steam turbines, will be capable of producing a further 55 MW. Discussions have been held with BC Hydro with a view to obtaining an agreement, as well as with a major utility company to provide operating, technical and financial support for the project. At full power, the energy island would burn approximately 250,000 tonnes per year. Gold River is approximately 70 kilometres west of the minesite, making transportation fairly easy by truck. In addition, the Gold River site has an excellent deep sea port from which it may be possible to ship to export markets.

- The potential economic maximization of our coal fines ponds remains an ongoing issue. We now believe that the highest and best use for this product is as a briquette, marketed to cement companies. The fines have an ash content of approximately 30%, with the ash consisting in the main of silica and alumina. Both these minerals are needed for cement raw material feed-stock. Formulating a binder to allow forming of the briquettes is now underway. It is estimated that Quinsam has approximately 350,000 tonnes of fines in its two settling ponds.

Financial Results & Operations

1999 net loss was $26.9 million (1.55 cents/share) versus a $9.6 million loss (0.54 cents/share) in 1998. The loss in 1999 can be mainly attributed to a one time write-down in the carrying values of the Company's assets and liabilities of $27.1 million as a result of the financial situation the company is in.

Revenue from coal sales fell to $14.9 million in 1999 from $29.7 million in 1998, a decrease of 49.8%. Tonnage sold during the year amounted to 354,000 MT (1998:684,000 MT). An average price of $42.01/MT was achieved in 1999 versus $43.42/MT in 1998, a decrease of 3.2%. However the income from coal operations in 1999 was $1,722,649 versus $350,594 in 1998.

Liquidity and Capital Resources

<u>Operating cash flow</u>:

Operating cash flow in 1999 was a negative $4.1 million, compared to negative $11.7 million in 1998.

Investing Activities

Only two significant capital expenditures were made in 1999, a rebuilt Fletcher roof-bolter which has proved to be an excellent addition to the Quinsam equipment fleet, and a new vent raise to provide improved ventilation in our new development areas. Total capital expenditures amounted to$692,000 in 1999.

Financing Activities

Approximately $0.4 million was raised in 1999 as follows:

- $1.1 million from Marubeni as their share of working capital support for Quinsam
- repayment of loans totalling $0.7 million.

Cash Resources and Liquidity

At year end 1999, the Company's cash balance amounted to $1.9 million.

Outlook

Quinsam's core competency is barge-loads of coal delivered to dock-side locations within the Pacific Northwest. We are constantly on the lookout for new sales orders to such locations. One new customer has been added to our customer base in 2000 and there are several prospective customers that are currently testing our coal specifications for potential orders. Bidding for a new contract for a super-compliant coal (0.25% sulphur) is expected in June 2000, and this will be the first time that Quinsam has been asked to bid by this company.

Risk Factors

Many of the risk factors previously identified have been significantly ameliorated or indeed, entirely removed. For example, with five year fixed price contracts with our major customers (with escalators), price risk has been all but eliminated. Operational risk, of course, is always present, but mitigated by the very high level of maintenance performed on our equipment fleet.

Safety is of primary importance and management continually stress the maxim that "Safety is Job # 1". In January 1999 we introduced a group and individual incentive program, and this has been enhanced for 2000. As well, safety training was further improved, and every underground miner has now completed the St. John's Ambulance First Aid Course.

Year 2000 Issue

The Company believes that to the extent determinable, its operations and systems are Y2K compliant. There have been no problems encountered to date with any of the Company's operations related to the Y2K issue. Although the change in date has occurred the Company continues to monitor its processes as well as those related to customers, suppliers and other third parties.

Hillsborough Resources Limited

Consolidated Financial Statements
December 31, 1999 and 1998

Together with Auditors' Report

AUDITORS' REPORT

To the Shareholders of
Hillsborough Resources Limited:

We have audited the consolidated balance sheets of **HILLSBOROUGH RESOURCES LIMITED** as at December 31, 1999 and 1998, and the consolidated statements of operations and deficit and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance 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.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 1999 and 1998 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Arthur Andersen LLP

Vancouver, British Columbia
May 5, 2000.

HILLSBOROUGH RESOURCES LIMITED
CONSOLIDATED BALANCE SHEETS
DECEMBER 31, 1999 AND 1998

	1999	1998
ASSETS (Note 1)		
CURRENT ASSETS		
Cash	$ 1,880,251	$ 4,401,383
Marketable securities (Note 2)	1,790,404	1,900,504
Receivables	1,525,791	1,387,172
Unbilled revenue	1,507,802	6,232,252
Inventories (Note 4)	676,229	1,591,945
Prepaid expenses	245,576	231,469
	7,626,053	15,744,725
CAPITAL ASSETS (Notes 5 and 7)	6,555,640	41,995,469
INVESTMENTS AND DEFERRED CHARGES (Note 6)	1,626,476	2,479,802
	$ 15,808,169	$ 60,219,996
LIABILITIES AND SHAREHOLDERS' EQUITY (DEFICIT)		
CURRENT LIABILITIES		
Bank operating loan	$ -	$ 6,597,609
Accounts payable and accrued liabilities	8,436,553	6,595,220
Current portion of loans and lease obligations (Note 7)	3,738,114	2,393,430
Convertible debentures (Note 8)	5,000,000	-
Income and resource taxes payable	57,817	58,803
	17,232,484	15,645,062
LOANS AND LEASE OBLIGATIONS (Note 7)	676,256	2,767,897
CONVERTIBLE DEBENTURES (Note 8)	-	5,000,000
OTHER LIABILITIES	241,141	232,391
DEFERRED INCOME TAXES	1,015,000	1,015,000
NON-CONTROLLING INTERESTS (Note 9)	1	11,983,011
	19,164,882	36,643,361
COMMITMENTS (Note 13)		
SHAREHOLDERS' EQUITY (DEFICIT)		
Capital stock (Note 10)	38,153,831	38,197,885
Contributed surplus	1,712,983	1,672,909
Deficit	(43,223,527)	(16,294,159)
	(3,356,713)	23,576,635
	$ 15,808,169	$ 60,219,996

Approved by the Directors:

.... Director

.... Director

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

HILLSBOROUGH RESOURCES LIMITED
CONSOLIDATED STATEMENTS OF OPERATIONS AND DEFICIT
FOR THE YEARS ENDED DECEMBER 31, 1999 AND 1998

	1999	1998
COAL REVENUES	$ 14,855,336	$ 29,687,244
COAL PRODUCTION EXPENSES	13,132,687	29,336,650
INCOME FROM COAL OPERATIONS	1,722,649	350,594
OTHER EXPENSES (INCOME)		
Depreciation, depletion and amortization	3,360,749	3,949,656
Corporate restructuring	1,483,871	2,292,381
General and administrative	1,124,908	2,522,123
Interest	959,095	1,357,815
Creditor arrangements	543,105	-
Write-down of marketable securities	-	1,854,244
Write-off of exploration mineral property	-	1,377,437
Other income, net (Note 11)	(450,426)	(390,640)
LOSS BEFORE TAXES AND OTHER ITEMS	(5,298,653)	(12,612,422)
PROVISION FOR (RECOVERY OF) INCOME AND RESOURCE TAXES (Note 12)	(41,767)	152,777
LOSS BEFORE WRITE-DOWN OF ASSETS AND LIABILITIES AND NON-CONTROLLING INTERESTS	(5,256,886)	(12,765,199)
WRITE-DOWN OF ASSETS AND LIABILITIES (Note 1)	(27,172,114)	-
NON-CONTROLLING INTERESTS	5,499,632	3,167,977
NET LOSS	(26,929,368)	(9,597,222)
DEFICIT, beginning of year	(16,294,159)	(6,696,937)
DEFICIT, end of year	$ (43,223,527)	$ (16,294,159)
LOSS PER SHARE	$ (1.55)	$ (0.54)
WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING	17,322,300	17,648,715

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

HILLSBOROUGH RESOURCES LIMITED
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 1999 AND 1998

	1999	1998
CASH FLOWS FROM OPERATING ACTIVITIES		
Net loss	**$ (26,929,368)**	$ (9,597,222)
Add (deduct) items not affecting cash		
Depreciation, depletion and amortization	**3,360,749**	3,949,656
Non-controlling interests	**(5,499,632)**	(3,167,977)
Write-down of assets and liabilities, net	**27,172,114**	-
Write-down of marketable securities	**-**	1,854,244
Write-off of exploration mineral property	**-**	1,377,437
Write-down of deferred charges	**583,693**	-
Recovery of deferred income taxes	**-**	(80,000)
Gain on disposal of investments and other assets, net	**(259,366)**	(40,420)
Reclamation provision	**8,750**	16,616
	(1,563,060)	(5,687,666)
Net change in non-cash operating accounts	**5,420,793**	(6,018,590)
	3,857,733	(11,706,256)
CASH FLOWS FROM INVESTING ACTIVITIES		
Capital asset additions	**(675,940)**	(2,760,047)
Investments and deferred charges	**21,453**	(2,872,899)
Proceeds from disposal of investments and other assets	**492,031**	2,306,928
	(162,456)	(3,326,018)
CASH FLOWS FROM FINANCING ACTIVITIES		
Loans and lease obligations, net	**(746,957)**	(318,238)
Shares issued for compensation	**-**	567,998
Common shares purchased for cancellation	**(3,980)**	(318,885)
Due to Marubeni Coal Canada Ltd.	**1,132,137**	2,062,221
Issuance of convertible debenture	**-**	5,000,000
	381,200	6,993,096
INCREASE (DECREASE) IN CASH	**4,076,477**	(8,039,178)
CASH (OVERDRAFT), beginning of year	**(2,196,226)**	5,842,952
CASH (OVERDRAFT), end of year	**$ 1,880,251**	$ (2,196,226)

Cash (overdraft) is comprised of cash, net of bank operating loan.

	1999	1998
CASH PAID DURING THE YEAR FOR		
Interest	**$ 600,000**	$ 1,186,000
Taxes	**-**	105,000

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

HILLSBOROUGH RESOURCES LIMITED
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 1999 AND 1998

1. NATURE OF OPERATIONS AND GOING CONCERN

These consolidated financial statements include the accounts of Hillsborough Resources Limited ("Hillsborough"), its 63% owned subsidiary, Quinsam Coal Corporation ("Quinsam"), its 79% interest in T'Sable River Coal Corporation ("T'Sable"), and its wholly-owned inactive subsidiaries, Mine Services International Inc., Can-Am Airlines Inc. and American Dorset Inc. (collectively referred to as the "Company"). The 37% non-controlling interest of Quinsam was owned by Marubeni Coal Canada Ltd. ("Marubeni") at December 31, 1999.

The accompanying consolidated financial statements have been prepared on the basis of accounting principles applicable to a "going concern", which assume that the Company will continue in operation for at least one year and will be able to realize its assets and discharge its liabilities in the normal course of operations.

Several conditions and events cast substantial doubt about the Company's ability to continue as a "going concern". On May 14, 1999, Quinsam obtained an Order from the Supreme Court of British Columbia pursuant to the *Companies' Creditors Arrangement Act* ("CCAA") seeking protection from its creditors. On May 20, 1999, Hillsborough, as a consequence of Quinsam filing for protection, also obtained an Order from the Supreme Court of British Columbia pursuant to the CCAA. The Orders were sought so that Quinsam could continue operating its mine while it negotiated with its senior lenders and other creditors to restructure its debts.

Quinsam submitted a Plan of Arrangement (the "Plan") to reorganize and refinance its operations, which was accepted at a meeting of creditors on March 14, 2000 and subsequently approved by the Court. However, the Plan remains subject to a number of conditions, as set out in the Information and Proxy Circular to the creditors of Quinsam, that are required to be fulfilled prior to the Plan being implemented. The significant conditions and approvals outstanding include the following:

(a) consent by the BC Transportation Financing Authority to a reduction in the price per ton of coal shipped by Quinsam which is required to be paid tb the BC Transportation Financing Authority;

(b) execution of a new collective bargaining agreement by the United Steelworkers of America, Local 9347, which extends the currently expired agreement on identical terms in relation to wages and related benefits for at least an additional three years, subject to a 10% deferral of wages for the next two years, together with a similar extension to the Company's non-unionized employees;

(c) deferral of 50% of the hydro charges for the Quinsam mine site for the next two years;

(d) deferral of 50% of the property taxes for the Quinsam mine site payable to the District of Campbell River for the next two years.

Management is working towards fulfilling the terms of the Plan. Under the Plan, each Quinsam general creditor will receive an amount which is equal to the lesser of (a) that general creditor's pro rata share of 25% of Quinsam's free cash flow generated over the two calendar years immediately after the implementation date, or (b) 20% of that general creditor's claim. At December 31, 1999, Quinsam's general creditors' claims totalled approximately $6.8 million which is reported as accounts payable. If the Plan is implemented, these liabilities will be reduced by approximately $5.4 million to $1.4 million.

In the event that the Plan cannot be implemented, management has been pursuing various financing options and has had discussions with interested investors and lenders who are performing due diligence reviews. It is not possible to predict the outcome of the uncertainties that the Company is presently in.

HILLSBOROUGH RESOURCES LIMITED
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 1999 AND 1998

1. NATURE OF OPERATIONS AND GOING CONCERN (Continued)

These financial statements do not reflect adjustments that would be necessary if the Company were unable to continue as a "going concern". While management believes that the actions already taken or planned, as described above, will mitigate the adverse conditions and events which raise doubt about the validity of the "going concern" assumption used in preparing these financial statements, there can be no assurance that these actions will be successful and no assurance that the Company will be able to continue as a going concern.

If the Company were unable to continue as a "going concern", then adjustments would be necessary to the carrying values of assets, the reported amounts of its liabilities, the reported revenues and expenses, and the balance sheet classifications used.

Write-Down of Assets and Liabilities

As a result of the financial situation that the Company is in, management has evaluated the carrying values of its assets and liabilities and has written down its assets and liabilities by approximately $27.1 million in 1999. The components of this write-down are summarized below:

	$ millions
Quinsam	
Capital assets, working capital and investments	$ 31.3
Due to Marubeni (Notes 2 and 9)	(7.6)
Hillsborough	
Capital assets of Hillsborough and T'Sable	3.4
	$ 27.1

2. SUBSEQUENT EVENTS

Significant events which have occurred subsequent to December 31, 1999 include the following:

Quinsam

Pursuant to an agreement dated February 11, 2000, Hillsborough acquired the following interests from Marubeni:

(a) 11,100,000 common shares and 37 Class A preferred shares in the capital of Quinsam, which represents 37% of the total shares of Quinsam, for $10,000;

(b) 37 common shares in the capital of T'Sable for $10,000;

(c) all of the unsecured loans advanced to Quinsam for $1;

(d) an option to participate in a joint venture between Hillsborough and T'Sable for $72,499.

As a result of the transaction described above, which became effective on February 29, 2000, Quinsam becomes a wholly-owned subsidiary of Hillsborough.

HILLSBOROUGH RESOURCES LIMITED
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 1999 AND 1998

2. SUBSEQUENT EVENTS (Continued)

Sale of Marketable Securities

On March 23, 2000, the Company sold a portion of its marketable securities with a cost of $1,500,000 for net proceeds of $3,450,000 for a realized gain of $1,950,000.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Use of Estimates

The preparation of financial statements in accordance with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingencies 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.

Revenue Recognition

Coal Revenue and Unbilled Revenue

Coal revenue is recognized upon production when processing is complete and sales contracts exist. Unbilled revenue is recorded at its estimated net realizable value.

Contract Revenue

Contract revenue is recognized as services are rendered and related contract costs are expensed as incurred, which approximates the percentage of completion method of income recognition. Claims by the Company arising out of contracts are generally recorded in the year such claims are resolved. Provisions are made for the full amount of anticipated losses in the period in which they are first determined.

Coal Inventory

Raw coal inventory and coal for which no sales contracts exist are valued at the lower of average cost and net realizable value.

Supplies Inventory

Supplies inventory is recorded at the lower of average cost and net realizable value.

HILLSBOROUGH RESOURCES LIMITED
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 1999 AND 1998

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Capital Assets

Quinsam Coal Mine

Commercial open pit mining operations commenced at the Quinsam Mine in April 1989, and commercial underground operations commenced in July 1990. Development and waste removal costs capitalized prior to the start of commercial operations, reduced by revenues during that period, are amortized using the unit-of-production method based on proven and probable reserves. Subsequent development and waste removal costs which are associated with an increase in capacity are capitalized and amortized using the unit-of-production method based on proven and probable reserves.

Costs associated with the Texada Island ship loading facility are amortized based on the estimated tonnage to be handled over the current mine plan.

Buildings, plant and equipment are recorded at cost. Depreciation for buildings and plant is provided on the straight-line method based on the estimated useful lives of the assets according to the current mine plan. Depreciation for equipment is provided on the declining-balance method based on the estimated useful lives of the assets. The depreciation rates range from 5% to 50%.

Exploration Mineral Properties

Investments in exploration mineral properties are recorded at cost. In those cases where exploration activities are conducted jointly with others, only the Company's proportionate interest in the related mineral projects is included in the financial statements. All costs of acquiring mineral properties are capitalized and related costs of financing, including interest, and exploration and development costs are deferred on a project basis.

When a property is put into commercial production, the related investment is amortized on the unit-of-production method. If the carrying value exceeds the anticipated net recoverable amount, the excess is charged to earnings immediately. If a project is abandoned, the investment is written off immediately.

The recovery of the carrying amount of exploration mineral properties is dependent upon the future commercial success of related properties or the proceeds of disposition.

Contracting and Administrative Assets

Contracting and administrative assets are recorded at cost. Depreciation is provided using the declining-balance method over the estimated useful lives of the assets. The rates applied to the principal classes of depreciable assets are as follows:

Buildings	5%
Furniture and fixtures	20%
Equipment	30% to 50%

HILLSBOROUGH RESOURCES LIMITED
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Write-Downs

Capital assets have been written down to their estimated net recoverable amount which is based on estimated future net cash flows from use together with their residual value.

Deferred Financing Costs

Deferred financing costs are costs incurred related to arranging the financing of Quinsam and the restructuring of the Company in 1995, and are amortized over a period from five to fifteen years. The unamortized balance at December 31, 1998 was written off in 1999.

Deferred Charges

Deferred charges are costs incurred related to long-term contracts and are being charged to earnings on a straight-line basis over the life of the contracts to which they relate.

Marketable Securities

Marketable securities are recorded at the lower of cost and market value. At December 31, 1999, marketable securities are recorded at cost of $1,790,404 (market- $2,387,205).

Income Taxes

The Company follows the deferral method of applying the tax allocation basis of accounting for income taxes.

Foreign Currency Transactions

Trade transactions denominated in foreign currencies are recorded in Canadian dollars at the exchange rate prevailing at the time of the transaction. Hedged transactions are recorded at the forward exchange contract rate.

Monetary assets and liabilities denominated in foreign currencies are converted into Canadian dollars at the exchange rate prevailing at the balance sheet date.

Reclamation and Site Restoration Costs

Estimated reclamation and site restoration costs are charged against income on the unit-of-production method based upon estimated mineable reserves. Ongoing reclamation activities are charged to earnings as incurred.

Financial Instruments

The Company's financial instruments consist of term deposits, marketable securities, receivables, accounts payable and accrued liabilities, loans and lease obligations and convertible debentures. Management estimates that the fair values of these financial instruments approximate their carrying values, unless otherwise noted.

HILLSBOROUGH RESOURCES LIMITED
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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4. INVENTORIES

	1999	1998
Coal	$ 416,104	$ 389,997
Supplies	260,125	1,201,948
	$ 676,229	$ 1,591,945

5. CAPITAL ASSETS

	1999	1998
Producing mining properties		
Quinsam Coal Mine		
Mine acquisition and development costs	$ -	$ 17,332,863
Texada Island ship loading facility	-	1,646,917
Buildings, plant and equipment	5,528,232	33,800,606
Deferred main development costs	-	2,765,938
	5,528,232	55,546,324
Exploration mineral properties	339	3,217,340
Contracting and administrative assets		
Land	25,463	74,745
Buildings	-	456,327
Equipment	2,351,018	6,732,458
Furniture and fixtures	162,690	162,690
	2,539,171	7,426,220
	8,067,742	66,189,884
Less		
Accumulated depreciation, depletion and amortization		
Mine acquisition and development costs	-	4,965,308
Texada Island ship loading facility	-	949,033
Buildings, plant and equipment	-	11,786,542
Deferred main development costs	-	256,021
Contracting and administrative assets	1,512,102	6,237,511
	1,512,102	24,194,415
	$ 6,555,640	$ 41,995,469

At December 31, 1999, capital assets include equipment under capital lease with original costs totalling $1,588,240 (1998- $3,290,354) and accumulated amortization totalling $962,330 (1998- $1,409,123).

HILLSBOROUGH RESOURCES LIMITED
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6. INVESTMENTS AND DEFERRED CHARGES

	1999	1998
Guaranteed investment certificates	$ 1,512,500	$ 1,472,500
Deferred financing costs	-	772,927
Deferred charges	113,976	234,375
	$ 1,626,476	$ 2,479,802

The guaranteed investment certificates have been lodged as security for mining permits and other obligations.

7. LOANS AND LEASE OBLIGATIONS

	1999	1998
Term loan, bearing interest at 10.14%, repayable in semi-annual instalments of $500,000, excluding interest, commencing November 15, 1996, with a balloon payment of $1,500,000 on the maturity date, May 16, 2000, secured by a fixed and floating charge on the Quinsam Mine property	$ 3,000,000	$ 3,000,000
Term loan, bearing interest at 6.2%, repayable in monthly instalments of $1,278, including interest, secured by a first mortgage on land, maturing on March 31, 2003	44,357	56,532
Obligations under capital leases of equipment	1,370,013	2,104,795
	4,414,370	5,161,327
Less- Current portion of loans and lease obligations	3,738,114	2,393,430
	$ 676,256	$ 2,767,897

Lease Obligations

Capital lease obligations at December 31, 1999 are denominated in Canadian dollars and have effective interest rates ranging from prime plus 1% to 15%.

Future minimum payments under capital leases of equipment, excluding interest, for each of the next four years, are as follows:

2000	$ 720,475
2001	363,806
2002	201,499
2003	84,233
	$ 1,370,013

HILLSBOROUGH RESOURCES LIMITED
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8. CONVERTIBLE DEBENTURES

On February 6, 1998, the Company issued and sold by way of private placement $5,000,000 of convertible unsecured subordinated debentures to a private company. The debentures bear interest at a rate of 6% per annum, payable semi-annually commencing on December 31, 1998, and are convertible at any time at the option of the holder into that number of common shares of the Company obtained by dividing the principal amount of the debentures to be converted by $1.15. Except in limited circumstances, the debentures are not redeemable until December 31, 1999. After such date, the debentures will be redeemable by the Company at the principal amount plus accrued interest subject to certain conditions.

Management has determined that no material value is attributable to the equity component of these convertible debentures; accordingly, the convertible debentures are presented as a liability on the balance sheet.

As at December 31, 1999, the holder of the convertible debentures has demanded full payment of principal and interest as a result of the Company being in default of the terms of the debenture which includes Quinsam seeking an Order pursuant to CCAA. Accordingly, the convertible debentures are classified as a current liability at December 31, 1999.

9. NON-CONTROLLING INTERESTS

	1999	1998
Non-controlling interest	**$ -**	$ 5,499,632
Due to Marubeni Coal Canada Ltd.	**1**	6,483,379
	$ 1	$ 11,983,011

(a) Non-controlling interest

Non-controlling interest represents Marubeni's interest in the carrying values of the net assets of Quinsam. As described in Note 2, subsequent to year end, Marubeni sold to Hillsborough its 37% non-controlling interest in Quinsam.

(b) Due to Marubeni Coal Canada Ltd.

During 1999, Marubeni made additional loans to Quinsam, which resulted in an amount due to Marubeni of $7,615,516 at December 31, 1999. As described in Note 2, subsequent to year end, Marubeni sold to Hillsborough these unsecured loans advanced to Quinsam for $1. Accordingly, in connection with the write-down of assets as described in Note 1, the amount due to Marubeni has been written down to $1.

HILLSBOROUGH RESOURCES LIMITED
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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10. CAPITAL STOCK

	Number of Shares	Amount
Authorized		
Unlimited number of common shares		
Issued and outstanding		
Balance, December 31, 1997	17,219,968	$ 38,768,243
Issued for compensation	638,200	567,998
Repurchased for cancellation	(516,800)	(1,138,356)
Balance, December 31, 1998	17,341,368	38,197,885
Repurchased for cancellation	(20,000)	(44,054)
Balance, December 31, 1999	**17,321,368**	**$ 38,153,831**

A Director and Employee Incentive Stock Option and Share Compensation Plan, approved by the Board of Directors, allows for options to be granted to directors and key employees to purchase common shares of the Company provided that the aggregate number of common shares reserved for issuance at the date of grant of any option does not exceed 10% of the total issued and outstanding common shares. The option price will be determined by the Board of Directors at the time an option is granted. The option price will not be less than the market price of the common shares less the maximum discount permitted by regulatory authorities.

At December 31, 1999, the Company has 1,692,500 options outstanding with exercise prices ranging from $0.07 to $1.00.

11. OTHER INCOME

	1999	1998
Contract revenue, net	**$ 35,463**	$ 196,722
Other, net	**194,690**	153,498
Gain on disposal of investments and other assets, net	**220,273**	40,420
	$ 450,426	$ 390,640

12. PROVISION FOR (RECOVERY OF) INCOME AND RESOURCE TAXES

	1999	1998
Provision for (recovery of) current income and resource taxes	**$ (41,767)**	$ 152,777
Provision for deferred income taxes	**-**	-
Provision for (recovery of) income and resource taxes	**$ (41,767)**	$ 152,777

HILLSBOROUGH RESOURCES LIMITED
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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12. PROVISION FOR (RECOVERY OF) INCOME AND RESOURCE TAXES (Continued)

The provision for income and resource taxes is analyzed in the following table to show the taxes that would be payable (recoverable) by applying statutory tax rates to the Company's pre-tax earnings (loss) and the taxes actually provided in the accounts.

	1999	1998
Loss before provision for income and resource taxes	**$ (26,971,135)**	$ (9,444,445)
Combined statutory tax rates	**45%**	45%
Expected tax recovery at statutory rate	**$ (12,137,000)**	$ (4,250,000)
Adjust for tax effect of		
Non-deductible items	**50,000**	77,000
Non-taxable portion of capital gains	**(49,000)**	(32,000)
Tax deductions and loss carryforwards not recognized	**(430,000)**	2,659,000
Write-down of marketable securities	**-**	834,000
Write-off of exploration mineral property	**-**	620,000
Write-down of assets and liabilities	**12,566,000**	-
Resource and large corporation taxes	**(41,767)**	152,777
Other	**-**	92,000
Provision for (recovery of) income and resource taxes	**$ (41,767)**	$ 152,777

At December 31, 1999, the Company has various tax deductions available to be utilized in future years; however, utilization of these deductions may be restricted due to reorganizations undertaken by the Company. The potential benefit related to these tax deductions has not been recognized in the financial statements.

13. COMMITMENTS

(a) During 1996, Quinsam completed the construction of the coal transportation, storage and loading facilities that were financed to $9,000,000 and are owned by the BC Transportation Financing Authority. Pursuant to a Project User Agreement, Quinsam has agreed to pay for the use of the facilities by way of a monthly usage fee determined by the volume of clean coal transported from the mine site for the period from September 1, 1996 to August 31, 2011.

(b) Quinsam entered into a haulage contract with a company to transport coal from the Quinsam mine site to the storage and loading facility at Middle Point for the period from January 1, 1996 to December 31, 2005.

HILLSBOROUGH RESOURCES LIMITED
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14. YEAR 2000

The Year 2000 Issue arises because many computerized systems use two digits rather than four to identify a year. Date-sensitive systems may recognize the year 2000 as 1900 or some other date, resulting in errors when information using year 2000 dates is processed. In addition, similar problems may arise in some systems which use certain dates in 1999 to represent something other than a date. Although the change in date has occurred, it is not possible to conclude that all aspects of the Year 2000 Issue that may affect the Company, including those related to customers, suppliers, or other third parties, have been fully resolved.

HILLSBOROUGH RESOURCES LIMITED

CORPORATE INFORMATION

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Arthur Fraser – Chairman *
David J. Slater *
Craig C. Smith*

* Member of the Audit Committee

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Craig C. Smith
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