Sullivan Mines inc. / 1985 Annual Report

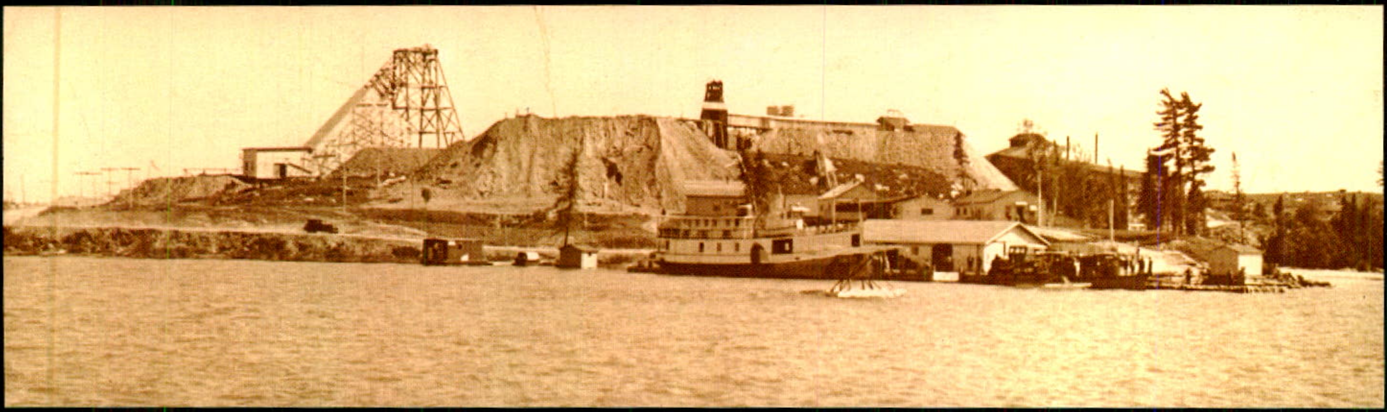
For over fifty years, the name Sullivan has been associated with numerous mining ventures in several regions of Quebec and New Brunswick. It all began with *Sullivan Gold Mines Limited.* (1929) which, after the acquisition of new mining properties, successively became *Sullivan Consolidated Mines Limited, Sullivan Mines Ltd., Sullivan Mining Group Ltd.* and, following its amalgamation with *East Sullivan Mines Ltd.* on July 1, 1983, became known by its present name: Sullivan Mines Inc.

These numerous reorganizations of the Sullivan operations reflect the constant concern for the Company's progress shown by its directors, officers and, in particular, its founder, Pierre Beauchemin. Progress has been ensured over the years by diversification of the Company's interests in several promising mineral regions, as well as through its involvement with the production of various minerals. Originally known as an important producer of precious metals – gold and silver – Sullivan became involved in the search for, development and exploitation of base metal deposits of copper, lead and zinc, while also producing lithium compounds and in partnership, tungsten concentrates.

It is only necessary to recall some of the Sullivan mining operations to indicate the scope of its activities during those years. The most important were those of Sullivan Mines Ltd., Quebec Lithium Corp., Hastings Mining and Development Co., and East Sullivan Mines Ltd. The recent amalgamation of the latter within the Sullivan Group contributed to the formation of the present Sullivan Mines Inc., which also includes several subsidiaries and affiliated companies such as Sullivan Resources Ltd., Sum Resources Inc., Brunswick Tin Mines Ltd., FEDPEN Ltd., and Courvan Mining Company Limited N.P.L.

The Sullivan installations as they looked over fifty years ago, at a time when the access road and railroad had not yet reached Val d'Or. Men, materials and vehicles were transported by boats and barges on the Harricana River from Amos to the site of mining operations on the shores of Dubuisson Lake.

Cover page:
Gold nuggets
(actual size)
extracted from the
placer at the
Valdez Creek Mine,
Alaska, U.S.A.



Company Profile

Sullivan Mines Inc., is a mining company currently engaged in the production of gold, as well as mining development and exploration of auriferous deposits jointly with other mining organizations.

Mining operations are conducted mainly in Canada, in the provinces of Québec and Ontario, and in Alaska, U.S.A.

Due to the diversity of its interests through participation in several mining ventures, and also its sustained efforts in the search for new deposits, Sullivan Mines Inc, hopes in the near future to add its name to the list of mining operators.

The Annual General Meeting of shareholders of Sullivan Mines Inc. will be held on Thursday, April 10th, 1986 at 10:00 A.M. at the Ritz Carlton Hotel, Sherbrooke Street West, Montréal, Québec.

Recent view of the Arthur W. White Mine installations in Ontario, being developed by the Dickenson-Sullivan joint venture.

Contents

Head Office:

Suite 800,
625 Dorchester Blvd. West
Montréal, Québec, H3B 1R2

Exploration Office:

775 – 3rd Avenue
Val d'Or, Québec, J9P 1S8

Registrar and Transfer Agent:

Guaranty Trust Company of Canada
Montréal – Toronto

Shares Listed:

Montreal Exchange/Toronto Stock Exchange

Eldrich-Flavel Project

Évain, Québec

Banker:

National Bank of Canada

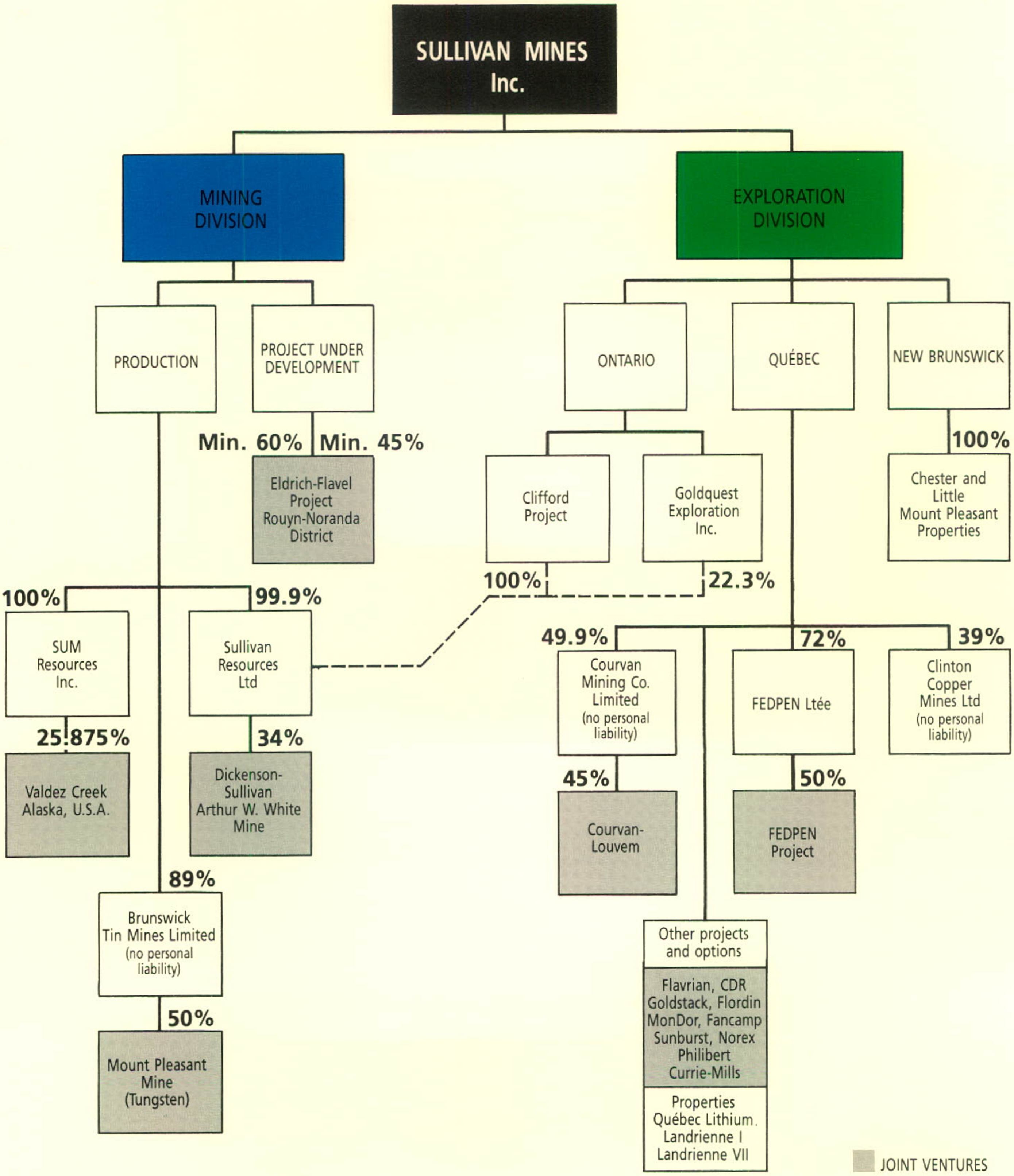
Auditors:

Maheu Noiseux

Note:

In this report, all amounts are in Canadian dollars and all tons are short tons of 2,000 pounds, unless otherwise indicated. A metric tonne is 1000 kilograms, or 2,204.6 pounds.

To convert "grams of gold per metric tonne into ounces per short ton", divide by factor 34.28.
One kilogram of gold is equivalent to 32.15 troy ounces.


SULLIVAN MINES Inc.
MINING DIVISION
EXPLORATION DIVISION
PRODUCTION
PROJECT UNDER DEVELOPMENT
ONTARIO
QUÉBEC
NEW BRUNSWICK
Min. 60%
Min. 45%
Eldrich-Flavel Project Rouyn-Noranda District
100%
Chester and Little Mount Pleasant Properties
Clifford Project
Goldquest Exploration Inc.
100%
22.3%
100%
SUM Resources Inc.
99.9%
Sullivan Resources Ltd
49.9%
Courvan Mining Co. Limited (no personal liability)
72%
FEDPEN Ltée
39%
Clinton Copper Mines Ltd (no personal liability)
25.875%
Valdez Creek Alaska, U.S.A.
34%
Dickenson-Sullivan Arthur W. White Mine
45%
Courvan-Louvem
50%
FEDPEN Project
89%
Brunswick Tin Mines Limited (no personal liability)
50%
Mount Pleasant Mine (Tungsten)
Other projects and options
Flavrian, CDR Goldstack, Flordin MonDor, Fancamp Sunburst, Norex Philibert Currie-Mills
Properties Québec Lithium. Landrienne I Landrienne VII
JOINT VENTURES

Directors' Report to the Shareholders

Claude Genest
President and Chief Executive Officer

Highlights:

/ Net earnings of $443,000., in comparison with a loss of more than $7.5 million for 1984.

/ Increased participation in the Valdez Creek joint venture project in Alaska.

/ Increased interest in Goldquest Exploration Inc. in Ontario.

/ Some $7 million in financing through flow through shares and a limited partnership.

/ Continuation of exploration and development of the Eldrich-Flavel project and increase of Sullivan's participation in view of the beginning of production during 1986.

/ Exploration work on some fifteen mining properties, several of which (Courvan, Mon Dor, Philibert, Fancamp and Goldquest) have produced interesting results.

/ Complete recovery of our investment – in less than three and a half years – in the Arthur W. White mine in Ontario.

/ Liquidation of the joint venture project at the Mount Pleasant tungsten mine in New Brunswick.

This report to the Shareholders marks another step in the continuous progress of Sullivan, which published its first annual report in 1933.

The fiscal year ended December 31, 1985 was a period for consolidating certain mining investments and putting in place the basic elements that will permit Sullivan Mines Inc. to set its course towards its principal objective: to rejoin the ranks of mining operators.

The financial results show net earnings in the amount of $443,000. ($0.05 per share) compared with a net loss of $7,519,000. ($0.94 per share) in 1984. Operating income stood at $1,217,000., against $2,453,000. in 1984. This reduction is mainly attributed to an increase in operating costs, spread about equally between the White Mine and the Valdez Creek operations. In the latter case, the full year's costs were charged to operations, while costs incurred prior to the start of the gold production in 1984 were capitalized. The costs increase at the White Mine reflects the general trend in mining. It is quite moderate and the White Mine is still among the few mines having an operating cost below $250 US an ounce. In fact, the 1985 cost of $240 US is about the same as in 1984.

The earnings were negatively affected by a rise in general administrative expenses resulting from an increase in personnel required by expanded activities. The higher administrative expenses also reflect a lower expense absorbtion rate, due to the fact that Sullivan contributed the share of exploration expenditures normally charged to one of the partners in the Eldrich-Flavel projects in return for an increase of our interest in this project.

During the year, certain mining investments were made in companies or projects of great potential, to be realized over the short or medium term. We increased our stake in the Valdez Creek gold placer to 25.875%. This project was initiated two years ago with the objective of self-financing a large exploration program in the Denali region in Alaska. The purpose was to block sufficient gold reserves in order to assure steady progress towards a profitable operation. If the gold price had not plummeted for the past two years, the operation would have produced a financial surplus accompanied by a complete technical success. The reserves outlined to date are large enough for a 10-year operation at the 1986 forecasted rate of production. In the short and medium terms, this interest in the Valdez Creek placer will be an excellent source of revenues for Sullivan with an annual production of approximately 11,000 ounces at a cost below $150 US per ounce, including exploration expenditures.

Our increased interest in Goldquest Exploration Inc. should be considered as a longer-term strategic investment. This company owns nearly 20,000 acres of mining property in the Red Lake area of Ontario. Dickenson Mines Limited is the largest shareholder of the company, a fact which increases the possibility of exploitation in case of a discovery. This region is one of the most prolific gold producing areas in the country. The geology of the Goldquest properties is very favourable, and the management is willing to pursue exploration of its properties in an aggressive manner. Now that the elements of success are in place, we believe that audacity, exertion and luck will do the rest.

During the 1985 fiscal year, exploration and development of the Eldrich-Flavel project encountered more problems than anticipated. The young team managing the property deserves to be the one that will undertake, we hope during 1986, the final development, followed by mining. The development of a new mine calls for intelligent use of all available means, a fair dosage of imagination, a great sense of entrepreneurship and much work. Those are all qualities that have contributed to the past success of the Sullivan group and that today should permeate all our activities aimed at assuring the continuity and progress of Sullivan Mines Inc. Our interest in the Eldrich property was increased to a minimum of 60%, and in Flavel to a floor of 45%, in consideration for financing the Soquem's 1985 share of exploration expenses.

For the first time in about 30 years, with the exception of Soquem's subscription of $8,250,000. beginning in 1981, the Company called on the public to finance its exploration and development programs. Private placements totaling $7,167,985. were subscribed on three different occasions. The first one was undertaken via a limited partnership, whose units were exchanged for 222,000 series "A" preferred shares, non-voting, non-participating, convertible and redeemable. This first issue contributed $3 million to the company's treasury. Concurrently, 434,240 flow through shares of which 150,000 will be issued in early 1986, for a consideration of $4,167,985, were subscribed on two occasions to a group of private investors. In both cases, tax benefits acted as the catalyst for this financing. Sullivan Mines Inc. intends to continue to study and develop financial packages that would simultaneously provide maximum tax benefits for investors, minimum dilution for the shareholders and optimum flexibility for the Company.

During the 1985 fiscal year, total cash flow from our 34% participation in the White Mine exceeded the cost of acquisition of our participation in July 1982, in the amount of $10,250,000. It is evident that the total recovery of our investment in less than three and a half years constitutes an excellent transaction for the Company. Furthermore, since acquiring this interest, under the competent management of our associate, Dickenson Mines Limited, the reserves, which stood at 612,000 ounces as at December 31, 1982, have been increased to 1,090,000 ounces at the end of 1985. This last figure does not include this year's new discoveries which, when fully evaluated, will add significantly to the wealth of this already important deposit. In 1986, we anticipate mine production of over 70,000 ounces, which means around 24,000 ounces for Sullivan. We are confident that in the next few years management will be in a position to increase production to 1,000 tons per day and to consider an optimum of 1,500 tons per day for the beginning of the nineties.

Numerous exploration programs were conducted during 1985. The Company wants to increase the activities during 1986, particularly to the extent that we would be in a position to initiate financing which will maximize the premium on the sale of the Company's shares through tax benefits. This recourse to outside sources of funds will be undertaken with the view of attracting new shareholders who will feel as strongly attached to the Company as those who, in some cases, have been with us for over a generation. To the present shareholders and those who will join them, we wish to stress the fact that Sullivan Mines Inc. is very well positioned to spread its wings in 1986, after many years of effort, perseverance and considerable daring.

If, as we strongly desire, the Eldrich-Flavel project begins to pay off during 1986, Sullivan Mines Inc. would be able to count on overall gold production in the order of 45,000 ounces in 1986, and even more in the following year. Under these circumstances, based on the market value of the shares at the beginning of the year, the capitalization for each ounce of gold produced would amount to $750, which represents a very conservative figure when compared with those applicable to other major gold producers in Canada.

It is always a sad occasion for anyone to attend the closure of a mining operation, particularly when, following great effort and large investments, this mine has just begun producing. As it is mentioned hereafter, the tungsten mine of Mount Pleasant, in which Sullivan Mines, through its subsidiary, owned a 50% interest in a joint venture, has put an end to its activities of recent years. Billiton Canada Limited has proceeded with the liquidation of the assets and properties of the joint venture. Mount Pleasant Resources Inc., owner of mining rights which were transferred to Brunswick Tin Mines Limited and from this latter company to the joint venture, has proceeded with a court action in the Supreme Court of Ontario against Billiton Canada Limited, Billiton Metals Canada Inc. and Brunswick Tin Mines Limited for damages amounting to $10 million, in respect of royalties which may become payable at some future time. According to our solicitors, this action is not founded in fact or in law and the Company is vigorously defending its position. The Company is taking proceedings to be indemnified by Billiton Canada Limited, Billiton Metals Canada Inc. and LAC Minerals Inc. against any liability which may be found against it.

Mr. Lucien C. Béliveau, who directed the company until May 1985, is now partly retired; he is still a member of the Board and acts as Vice-Chairman. Mr. Béliveau, who has been associated with Sullivan since 1942, is the perfect example of a competent and dedicated professional whom we wish to emulate. We thank him most sincerely for his valuable contribution to what has become Sullivan Mines Inc. Mr. Pierre J. Boudreault resigned during the past year as a Director and also as Vice-President Mines. We regret the departure of this competent engineer who was highly regarded and esteemed in our organization. Mr. Paul J. Bourassa, to whom we extend a warm welcome, has succeeded him on the Board of Directors.

The cooperation of all employees is highly appreciated. Their competence, integrity and constant devotion to duty are the source of our success and a guarantee for the future. We would like to thank them most sincerely on your behalf and on behalf of the Company.

ON BEHALF OF THE BOARD OF DIRECTORS,

Claude Genest
President and Chief Executive Officer

J.-J. Beauchemin, Q.C.
Chairman of the Board

March 1st, 1986

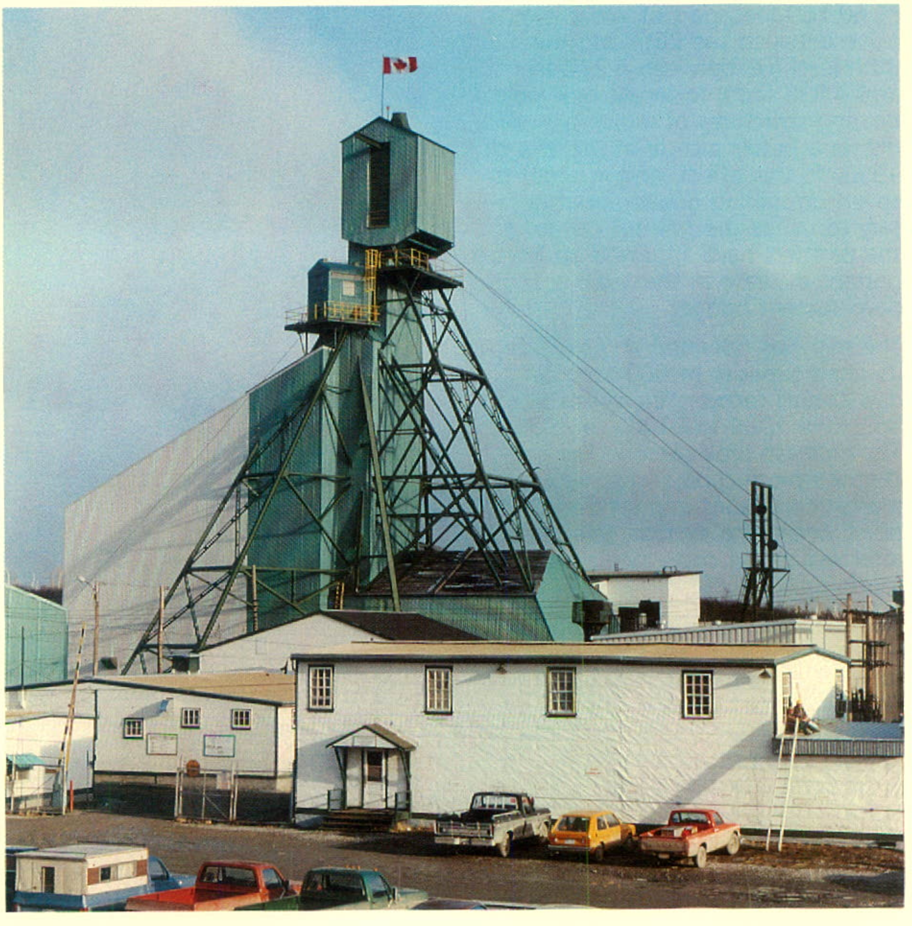
Mining Division
1. Production

a) Sullivan Resources Ltd.

(incorporated under the Ontario Business Corporation Act.)
The Arthur W. White Mine,
Balmertown, Ontario
Dickenson – Sullivan Joint Venture

Mining Operations Review	1985	1984	1983
Tons of ore milled	**215 140**	206 800	206 000
Average grade milled ounces of gold per ton	**0.33**	0.34	0.31
Recovery – bullion %	**83.6**	83.8	82.4
Recovery – bullion and concentrate %	**87.4**	86.2	86.2
Production of gold, in ounces – bullion	**59 978**	58 936	51 865
Production of gold, in ounces – concentrate	**2 757**	1 834	—
Total production	**62 735**	60 770	51 865
Sullivan Resources Ltd. Share: 34%			
Production of gold, in ounce – bullion	**20 393**	20 038	17 634
Production of gold, in ounce – concentrate	**937**	624	—
Total production	**21 330**	20 662	17 634
Average sale price $ Cdn per ounce of gold bullion	**451**	475	538
$ Cdn per ounce of gold (net of realization cost) – concentrate	**175**	40	—
Average	**438**	462	538
Operation cost per ounce, $ Cdn	**328**	310	307

Location of
Arthur W. White Mine



Headframe of
the Arthur W. White mine,
Balmertown, Ontario

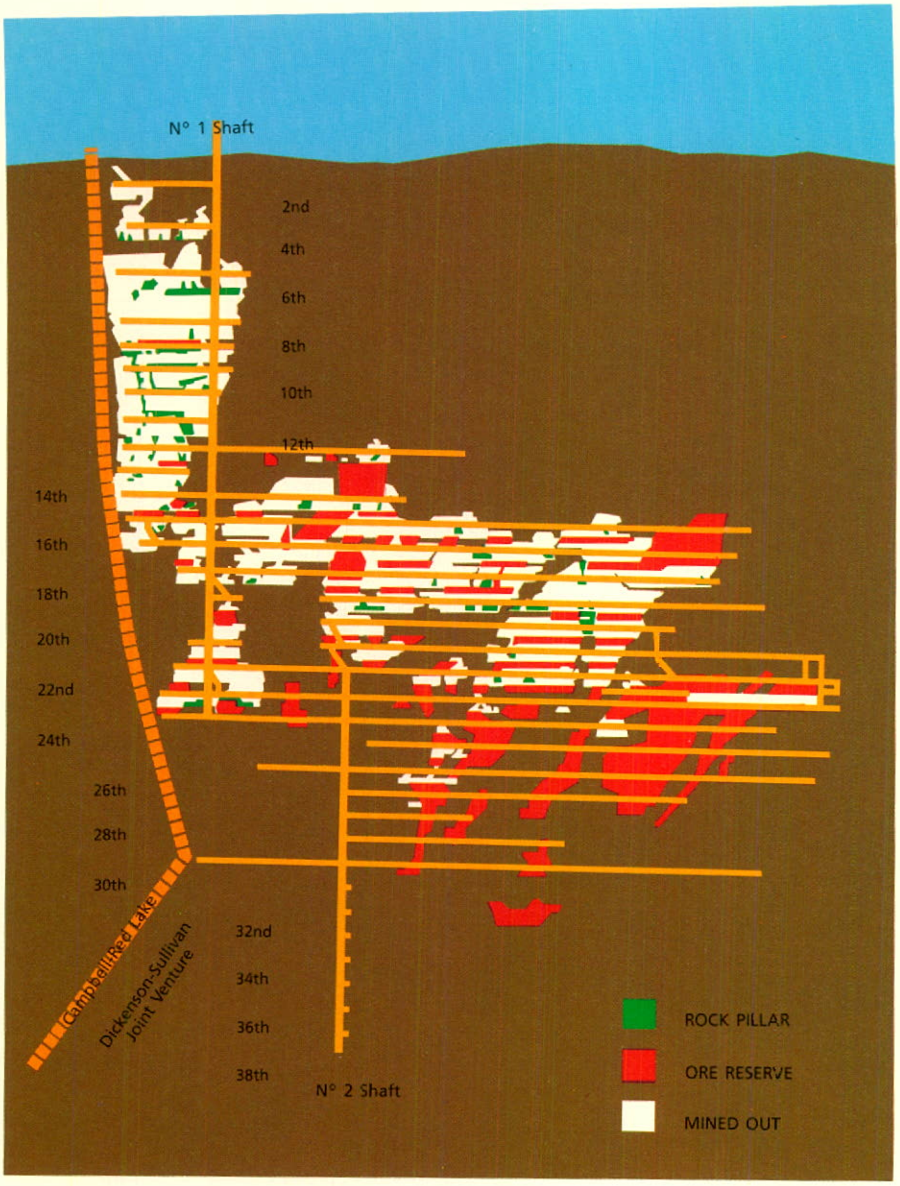
During the fiscal year ended December 31, 1985, the Arthur W. White Mine, in which Sullivan Resources Ltd. has an undivided 34% interest, treated 215,140 short tons of gold ore grading 0.33 ounces of gold per ton, and produced 59,978 ounces of gold bullion and 2,757 ounces in concentrate. Compared to the previous year, gold production increased 3%. The 1986 forecast indicates that production will exceed 70,000 ounces, thus increasing our share of production by more than 12% over 1985.

The ore is mined by the cut and fill method, with 97% coming from production stopes and the rest from development. The backfill plant produced and sent underground 85,000 tons of material for consolidation of empty stopes.

The mine development required 3,126 feet of drifts and cross cuts and 1,652 feet of raising. This represents an increase of 7% over 1984. Underground drilling consisted of 60,760 feet, part of which was done between the 26th and the 30th level (i.e. between 4,238 feet and 4,838 feet), to locate new gold bearing structures of which we will obtain a better picture at the end of 1986. To this effect, and in order to speed up mining development necessary to utilize the full mill capacity, the partners have approved an important increase in the 1986 development budget.

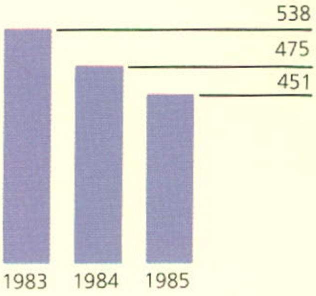
The mill was operated at 73.6% of its rated capacity of 800 tons per day. Overall recovery increased from 86.2% in 1984 to 87.4% in 1985. The increase took place in the concentrate production sector, where market conditions improved to the point where the average sale price after realization costs increased fourfold.

The operating costs before amortization stood at $ 96. per ton, equivalent to $ 328. per ounce of gold ($ 240. US). The 5.49% cost per ton increase has been compressed to 2.82% when applied to ounces of gold produced, those being in progress over 1984.



Longitudinal Section — Typical Zone

Average Gold Sale Price



Sullivan sold its share of gold production at an average price of $ 451. ($ 329. US) per ounce, compared to an average of $ 475. in 1984 and $ 538. in 1983. During 1985, the London gold average (second fixing) was $ 433. ($ 317. US) per ounce, fluctuating from a low of $ 285. US on February 25 to a high of $ 340. US on August 28.

The 7.98% drop in our average sale price translates into a reduction of 2.08% in our revenues. Coupled with the cost increase, this reduction compressed cash flow from our participation in the White Mine by a factor of 25% compared to 1984.

	Profit Variation 1985/1984 % of Variation		
	Total	**Per Ton**	**Per Ounce**
Revenues	— 2.08	— 5.88	— 7.98
Costs	+ 9.02	+ 5.49	+ 2.82
Cash Flow	—24.78	—28.89	—29.94

As at December 31, 1985, the proven, probable and possible ore reserves* after dilution where as follows:

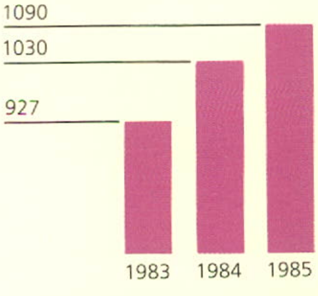
	In thousands of short tons		
	1985	1984	1983
Proven	**1,532 @ 0.35 oz**	1,240 @ 0.332 oz	1,151 @ 0.343 oz
Probable	**1,383 @ 0.27 oz**	1,233 @ 0.317 oz	874 @ 0.293 oz
Possible	**671 @ 0.28 oz**	810 @ 0.279 oz	1,006 @ 0.275 oz
Total	**3,586 @ 0.304 oz**	3,283 @ 0.314 oz	3,031 @ 0.306 oz

*As established by Arthur W. White Mine geological personnel

After mining 215,000 tons in 1985, ore reserves increased by 333,000 tons or, expressed in ounces, 60,000 gold ounces, without considering the new ore zones discovered during the year, to which we refer above. We feel that these new zones will prove to be important ones.

At December 31, 1985 the White Mine had a total of 278 employees. During the year, all personnel previously lodged in bunkhouses were relocated in new housing facilities, better suited for today's living conditions. Labour relations remain excellent. The mine rescue team won the Ontario Provincial Mine Rescue Competition for 1985.

Ore reserves expressed in gold ounces (in thousands)



Definitions:

1. Proven ore: Ore which has been partially developed by one or more mine openings along zones with demonstrable geological continuity, and in which grade has been established by chip sampling or by two or more diamond drill holes. Limits of 25 feet on either side of the openings are assumed.
2. Probable ore: Ore which has been indicated and sampled by a diamond drill hole within a zone of demonstrable geological continuity, or ore which falls within 50 feet of a mine opening as used in defining "Proven Ore".
3. Possible ore: One that is contiguous to proven and probable ore within interpreted geological zones but which has not been sampled.

Alaska: beauty, bounty and a challenging climate.

b) SUM Resources Inc.

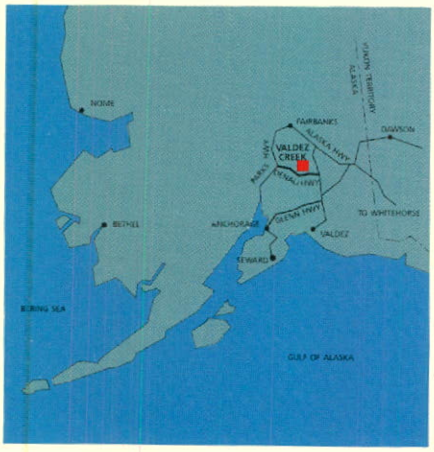
Wholly-owned subsidiary incorporated under the laws of Texas, U.S.A.
Valdez Creek Mine, Alaska, U.S.A.
Barrick-Camindex-Sullivan Joint Venture.

Mine Operations Review	**1985**	1984
Cubic yards of gravel removed	**1,177,000**	835,000
Cubic yards of pay gravel treated	**304,000**	179,000
Average grade (oz/c.y.)	**0.098**	0.11
Ounces recovered (raw gold)	**29,823**	19,754
Ounces recovered (fine gold)	**25,163**	16,787

SUM Resources Inc. share: 25.875% (13.875% prior to Nov. 1, 1985)

Ounces of fine gold	**3,491**	2,330
Average sale price $ Cdn. per ounce	**428**	424
Operation cost $ Cdn. per ounce	**353**	*

*Not comparable.



Location of Valdez Creek Mine, Alaska, U.S.A.

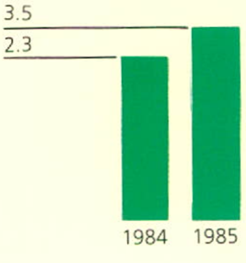
During the 1985 fiscal year, the Valdez Creek Mine, in which Sullivan Mines Inc., through its wholly owned subsidiary SUM Resources Inc. has a 25.875% interest (13.875% prior to Nov. 1, 1985), produced 25,163 ounces of fine gold compared to 16,787 ounces the previous year. The rugged Alaska climate restricts production to a short, seven-months period, from April to October. In 1986, total production in excess of 40,000 ounces is forecasted. The added output, coupled with our increased participation, will multiply our share of production by a factor of 3.2 compared to 1985.

The gold occurs in gravels deposited in ancient riverbeds known as channels. The richest concentration is closest to bedrock. The reserves are mined readily by open-pit method, using ordinary excavating equipment and with only very little drilling and blasting being required.

The raw gold is recovered without crushing, after screening, washing and sluice box separation. Final recovery is by gravity separation. All in all, it is a relatively simple operation.

During the last mining season, 1,177,000 cubic yards of waste gravel were excavated from four (4) channels, compared with 835,000 cubic yards in 1984.

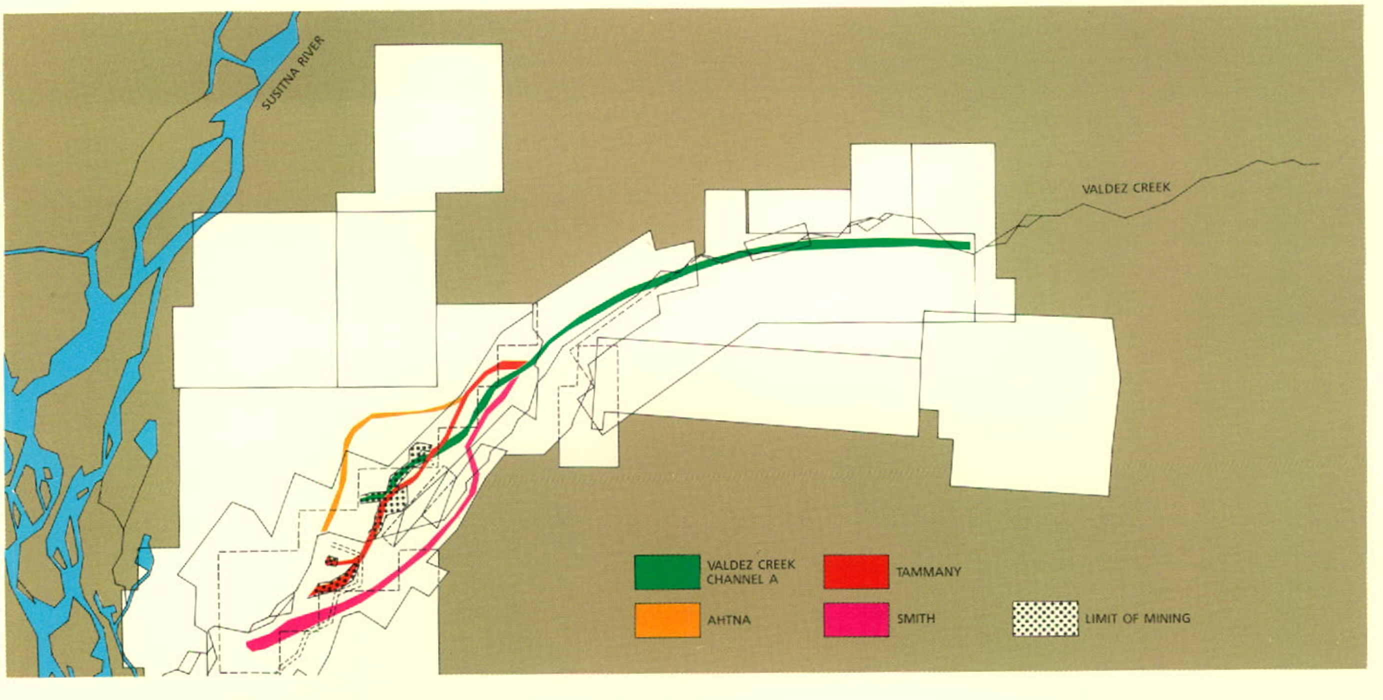
Gold ounces (in thousands)



The plant treated 304,000 cubic yards of pay gravel, from which 29,823 ounces of raw gold were extracted. Refining outside the property allowed for the production of 25,163 fine ounces of gold. During 1984, the tune-up year, 179,000 cubic yards were treated, from which 19,754 ounces of raw gold and, subsequently, 16,787 ounces of fine gold were extracted.

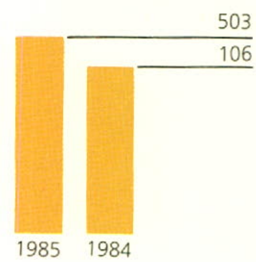
The sum of $ 1,000,000 US was invested in exploration during 1985, approximately the same amount as in 1984. Ground exploration consists of refractory seismic surveys which establish the location and direction of the ancient river channels in the bedrock. Once located, these channels are then drilled using reverse circulation drills. The samples extracted by this drill process on a given grid are then used as a basis to establish the grade and size of the ore reserves. During the 1985 season, 183 holes totaling 23,607 feet were drilled, in order to assess various channels over a distance of 13,500 feet.

Gold Bearing Channel Deposits of Valdez Creek



Mining of pay gravel, Valdez Creek gold placer, Alaska

Ore reserves expressed in gold ounces (in thousands)



As of December 31, the proven, probable, possible and inferred ore reserves* were as follows:

*As reported by W.G.M. Inc., Consulting Engineers.

In thousands of cubic yards		
	1985	1984
Proven	**406 @ 0.129 oz**	798 @ 0.088 oz
Probable	**801 @ 0.081 oz**	
Possible	**2,996 @ 0.087 oz**	594 @ 0.060 oz
Inferred	**1,739 @ 0.071 oz**	—
TOTAL	**5,942 @ 0.085 oz**	1,392 @ 0.076 oz

After extracting 304,000 cubic yards, ore reserves were increased by 4,554,000 cubic yards and 397,000 ounces of gold.

The personnel varies according to the activity. There were 38 employees in April 1985, increasing to a peak of 99 in July. No serious accident was reported during the year. The social climate is excellent and free from labour conflicts.

Definitions:

Proven reserves: Proven reserves are those fully delineated by drill sections with holes spaced no more than 50 to 60 feet apart and flanked by adjacent drill sections defining similar, correlatable results.

Probable reserves: Probable reserves are those where the distance between drill sections exceeds 250 feet (generally 500 or more feet) or where drill hole spacing along the section exceeds 75 feets (generally 100 foot spacings).

Possible reserves: Possible reserves are those where the drill lines are spaced more than 500 feet apart of where only one drill hole intersected a gold-bearing channel that could be correlated between wide-spaced drill lines.

Inferred reserves: Inferred reserves are those based on projection of the known paleochannels beyond the areas tested by drilling where there is reasonable confidence of their presence.

c) Brunswick Tin Mines Limited

Incorporated under part III of the New Brunswick Companies' Act. Mount Pleasant Tungsten Mine. Billiton-Brunswick Tin Mines Joint Venture.

Concurrently with the closing of the mine at the end of July 1985, our partners, Billiton Canada Limited proceeded with liquidation of the assets and properties of the joint venturers.

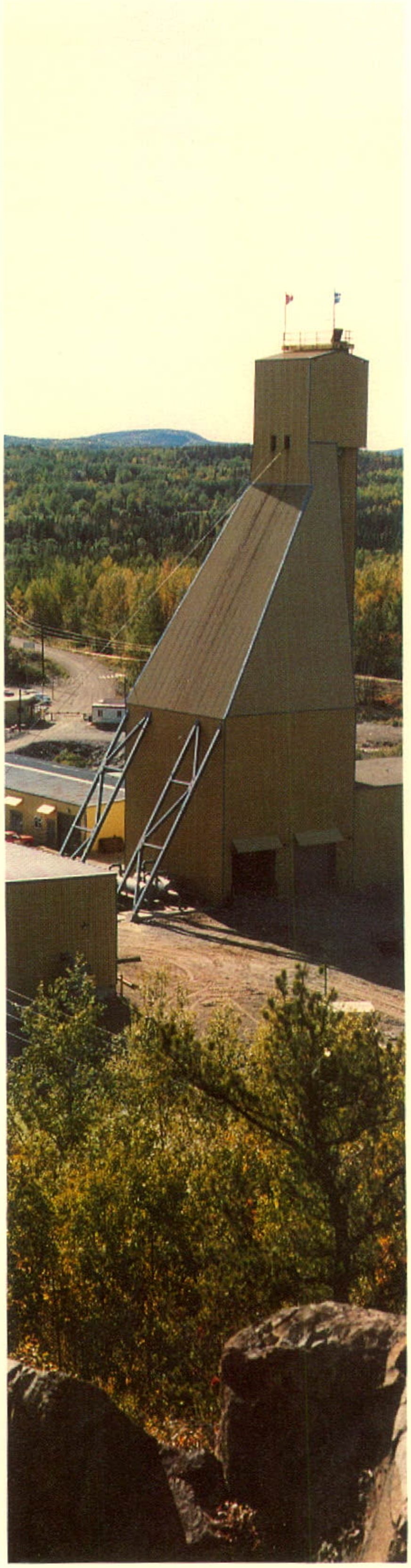
In 1984, faced with the unlikelihood of earning any revenue from its participation, the Company decided to write off the $ 9,712,000 invested in this project through the years by Brunswick Tin Mines Limited.

2. Project Under Development

Eldrich-Flavel project

Rouyn-Noranda District – Province of Québec
Soquem-Aiguebelle Resources Inc.-Sullivan Joint Venture

Location of Eldrich-Flavel project



Headframe of Eldrich-Flavel project, Québec

This project, initiated in July 1984, was continued throughout the year and, under normal conditions, should be completed by the 1986 spring season. Only then will a decision be taken on the future of these properties.

This project consists of two adjoining properties. The first, Eldrich, is owned by Soquem and Sullivan in proportion to the expenditures financed by each party. At December 31, 1985, the respective interests of Sullivan and Soquem were 78% and 22%. The second property, Flavel, generally follows the same sharing rules, and at the same date, the interests were split 25%, 20% and 55% respectively for Aiguebelle, Soquem and Sullivan. During 1986, by catching up on the financing of past work, Soquem could increase its interest to 40% in Eldrich and 30% in Flavel.

Mine dewatering and rehabilitation of the shaft and stations have been completed. The installation of the hoist, compressors and head frame was completed so that all systems were operational during the 3rd quarter of 1985.

During the year, in addition to those mentioned above, the following works were performed:

Exploration and Development (In meters)

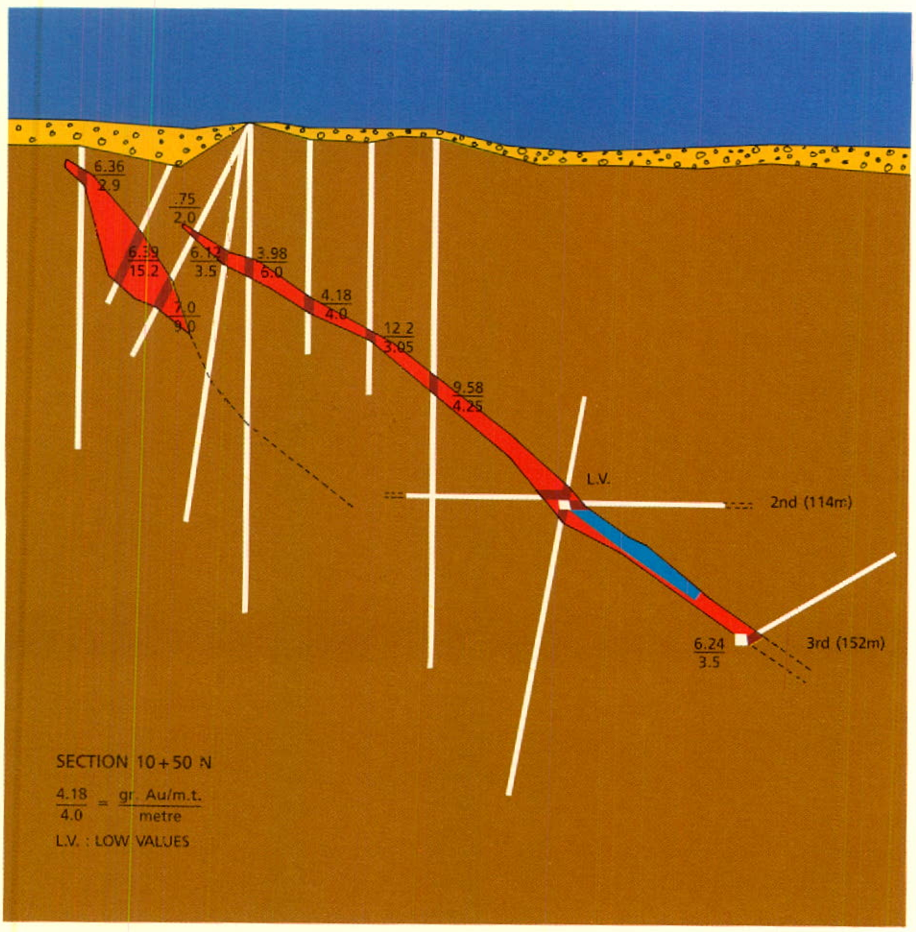
	Budgeted	**Actual**
Surface drilling	6,373	17,048
Underground drilling	16,474	21,496
Rehabilitation of drifts	2,513	2,902
New drifts	2,280	1,435
Raises	1,387	362

The work progress was slower than anticipated. Two reasons explain the delay. First, the old underground workings were in a poorer state than expected. This called for additional rehabilitation and more caution on the part of the crew, thereby reducing the rate of advance. Secondly, the impression that the ore grade could be lower than first estimated required additional underground drilling. When not feasible due to lack of drilling stations, surface drilling was then substituted. The immense scope of work, the lack of ore passes, combined with the fact that the mine covers a wide area, all contributed to logistic problems without easy solution, therefore causing delays.

In order to establish an optimum coefficient of confidence in the ore grade, a bulk sample from 3 stopes will be treated with the aim of establishing a better correlation between grade derived from drilling, raising and mining.

The 1985 program called for an investment of $ 9,255,985 from the associates, split as to $ 6,405,872 on the Eldrich property and $ 2,850,113 for Flavel. To bring the project to the feasibility study stage, an additional $ 2,500,000 investment is needed in 1986.

At year end, personnel numbered 90 employees, including 25 staff. A request for certification of hourly paid employees by the "Metallurgistes Unis d'Amérique", deposited in September 1985, has been granted by the Commissaire général du travail. A 3 year labour agreement was negociated and signed by the parties in February 1986.



Eldrich-Flavel Project

Properties/Projects	Description	Activities and Prospects
QUEBEC		
Rouyn-Noranda District		
FLAVRIAN OPTION Soquem: 37.5% (management) Sullivan : 37.5% Aiguebelle Resources Inc.: 25.0%	Property located in Beauchastel and Duprat twps. It is well located, since it surrounds the former Win-Eldrich and Sunburst gold producing mines where Sullivan also has some interests. Several gold bearing zones are known to exist on the property.	The 1985 exploration program was confined mostly to diamond drilling investigation of the northern and southern extensions of the Eldrich-Flavel mineralized structures. No economic auriferous lens was outlined. During 1986, emphasis will be put on the exploration of gold bearing zones not related to the Eldrich-Flavel deposit.
SUNBURST PROJECT Sullivan : 25% (management) Soquem: 25% Sunburst Exploration Ltd.: 50%	Former gold producer located on Range I of Duprat twp. at 4 kms south of the Eldrich-Flavel gold deposit. The exploited ore body along the Quesabe fault is still open at depth and westward. This property produced some 90,000 m.t. at 10 gr. Au/m.t. between 1950 and 1952.	Diamond drilling on three different targets failed to show gold bearing lenses in 1985, despite some encouraging indications. It has been estimated that it could be possible to outline 360,000 m.t. at 6.3 gr. Au/m.t. across 1.5 m. by undertaking underground exploration work at depth. This could be interesting only in the event of higher gold prices and if the Eldrich-Flavel project goes ahead with its own concentrator.
C.D.R. OPTION Sullivan: 50% (management) C.D.R. Resources Inc.: 50%	Property located on Range X of Beauchastel twp. Previous work has shown the presence of a small deposit with 51,600 m.t. at 5.22 gr. Au/m.t.. The deposit could be made easily accessible by means of a ramp.	No action during 1985. The property is being kept in good standing pending favourable gold prices and a go-ahead decision on the Eldrich-Flavel deposit located some 10 kms to the northwest.
Val d'Or – Amos District		
CROINOR PROJECT Sullivan: 50% (management) Dominion Explorers Inc.: 50%	At least four gold bearing zones are known on this Pershing twp. property. According to present estimates, the most important one contains 386,000 m.t. at 5.48 gr. Au/m.t. after dilution. It has been investigated underground to a depth of 152 meters through the facilities of four levels and a ramp to the first level. The three other gold zones are not well known.	Surface stripping down to bedrock and metallurgical investigations were conducted in 1985 on the main zone (diorite). For 1986 it is proposed to investigate by diamond drilling: a) the northern contact of the porphyry over a length of 1.6 km. Three holes drilled in the past have yielded: 6.05 gr. Au/m.t. over 2.3 m. 10.63 gr. Au/m.t. over 1.5 m. 27.78 gr. Au/m.t. over 1.0 m. b) a graphitic zone containing smokey quartz veins. One prior hole gave 17.5 gr. Au/m.t. over 1.52 m. on this zone.

Properties/Projects	Description	Activities and Prospects
GOLDSTACK OPTION Sullivan: 50% (management) Goldstack Resources Ltd.: 50%	The property is part of the previous Malartic Goldfields mine in Dubuisson twp. Complementary to an ill defined residual tonnage within the mine area, the nearby south Briar zone has 185,000 indicated m.t. at 5.66 gr. Au/m.t..	No work done during 1985 because of weak prices for gold. Resumption of activities is planned for 1986.
COURVAN PROJECT Courvan Mining Company Ltd.: 45% Société Minière Louvem Inc. N.P.L.: 55% (management)	This project is important. Sullivan has nearly 50% interest in Courvan Mining Company Ltd. The property is located in the northwestern corner of Louvicourt twp. Its major feature is a gold bearing structure known as the "southwest zone" where efforts are being made to determine the structure of the gold veins.	Detailed geochemical and geophysical surveys were conducted in 1985. This program was followed by diamond drilling intended to gain a better understanding of the mineralized structures. Activities will be continued in 1986. Results obtained to date are very encouraging.
QUEBEC LITHIUM PROPERTY Sullivan: 100%	Former lithium producer; this property located in Lacorne twp. also shows interesting geological structures which could have been gold bearing.	Detailed geophysical surveys done in 1985 revealed the presence of an anomalous zone which was tested at depth by one drill hole. The sulfures encountered were barren and investigations were suspended.
LANDRIENNE PROPERTIES Sullivan: 100%	These two properties located in the Landrienne twp. were staked in 1985. They contain shear zones on which airborne conductors have been pinpointed.	Ground geophysical surveys initiated during 1985 will be completed in the current year. The results will permit verification of the anomalies to determine whether or not following up drilling is warranted.
Chibougamau District		
MONDOR OPTION Sullivan: 70% (management) Explorations Mon Dor Inc.: 30%	The MONDOR property covers parts of Brongniart, Rasles, Hauy and Fancamp twps. Several indications of gold mineralization have been identified. The higher values are: 5.5 gr. Au/m.t. over 3.04 m. and 6.86 gr. Au/m.t. over 1.52 m.	Stripping and sampling were undertaken during 1985. The results permitted a better understanding of the auriferous zones, which will be evaluated by drilling during 1986.

Properties/Projects	Description	Activities and Prospects
PHILIBERT PROJECT Soquem: 60% (management) Sullivan : 40%	Gold property extending over the townships of Fancamp, Gamache and Hazeur. The investigation of some mineralized blocks on surface has identified a favourable area for gold mineralization. The best values obtained have been 7.03 and 10.92 gr. Au/m.t. over 1.0 m. and 4.21 gr. Au/m.t. over 3.0 m. in three different holes spaced at 40 metres each.	Geophysical surveys, stripping and drilling pursued during the year showed the presence of a geological contact (silicified) where gold mineralization has been found by drilling. Still early to evaluate the project; more work being planned for 1986.
FANCAMP PROJECT Soquem: 50% (management) Sullivan : 50%	This gold-bearing property covers parts of the townships of Fancamp, Gamache and Hazeur, a few kilometres west of the Philibert project and 5 kms south of MONDOR project. Some gold in smokey quartz has been found in 1984.	Geophysical surveys and diamond drilling executed during 1985 have given excellent results along a shear zone. The best values in different holes have shown: 68 gr. Au/m.t. over 1.52 m., 10.97 gr. Au/m.t. over 1.0 m. and 4.97 gr. Au/m.t. over 2.9 m. It is still early to evaluate the importance of this discovery, but more work is planned for 1986.
CURRIE-MILLS PROJECT Sullivan : 45% (management) S.D.B.J. : 40% M. Currie-Mills: 15%	This deposit, located near the Joe Mann gold property (Meston Lake and CAM-CHIB) has only been submitted to preliminary investigation. The mineralogy and geological structure are similar to the Joe Mann formations.	No new activity in 1985. Indicated reserves are still at 62,632 m.t. with 4.25 gr. Au/m.t. (north zone) and 105,285 m.t. with 2.06 gr. Au/m.t. (south zone). Additional drilling is contemplated for 1986.
Quevillon District		
FLORDIN PROJECT Sullivan : 50% (management) Soquem: 50%	The Desjardins township property contains a gold deposit evaluated at 471,000 m.t. at 6.65 gr. Au/m.t. across a width of 1.95 m.	Inactive during 1985. New activities are planned for 1986 over three mineralized zones.
Eastern Townships and Gaspesia District		
NOREX PROJECT, Eastern Townships Noranda Exploration Canada Limited: 60% (management) Sullivan: 40%	In 1983, Sullivan granted an option for a three-year period over all its mining properties in the Eastern Townships. These mining properties are located in the townships of Weedon and Stratford. In those optioned properties Sullivan has an interest of 40% of which 25% is participating. In properties acquired after the agreement, Sullivan has a 15% participating interest.	Inactive during 1985. There may be a renewal of activities in the coming year.

Properties/Projects	Description	Activities and Prospects
FEDPEN PROJECT, Gaspesia Sullivan : 50% Soquem: 50% (management)	This is the old FEDPEN zinc property in Lemieux township. Soquem can acquire a 50% interest with $450,000 of various exploration work over a period of five years (beginning in 1985).	This year's operations consisted of trench sampling and other surface work, followed by the compilation of drill results obtained. Four holes were drilled for a total length of 2,433 metres. Although two favourable horizons have been identified, no significant mineralization has been detected.
NEW BRUNSWICK		
LITTLE MOUNT PLEASANT PROPERTY Sullivan Resources Ltd.: 100%	Property located in the vicinity of the Mount Pleasant Mine.	A geochemical survey undertaken for statutory requirements has not produced any interesting results. It has been recommended that this property be abandoned since the Mount Pleasant Tungsten Mine is closed.
ONTARIO		
CLIFFORD PROJECT Sullivan Resources Ltd.: 100%	The property comprises 39 mining claims staked in Clifford township during the fall of 1985. The objective was to explore a small granitic stock of acid volcanic rocks. The Clifford township is located in Ontario near the Quebec border on the Porcupine-Cadillac axis.	General prospecting and geological work is recommended for 1986.
GOLDQUEST PROJECT, Red Lake District Interest of Sullivan Resources Ltd.: 22.3% in Goldquest Exploration Inc.	The Goldquest project covers a group of 12 mining properties in the Red Lake district. Each year, an average of $1 million of exploration work is spent on this project.	In 1985, the exploration program was mainly directed to the Abino property, which appears to be the most promising of the Goldquest group. The drilling has given very encouraging results and new auriferous zones have been discovered. To date, the size of the zones encountered are not very large, but the values obtained are high and consistent. Additional detailed work is planned for 1986.

Remark: Abandoned projects.
Certain projects, having shown no interesting results, were abandoned during 1985: including the options on Achates (Quevillon) and Villebon (Val d'Or – Amos), as well as the Launay, Malartic South and Malartic Nickel projects. However, sufficient statutory assessment work has been accumulated for the latter properties to keep them in good standing.

sullivan

Sullivan
Mines
Inc.

Financial Statements

sullivan

Sullivan Mines Inc.
(Incorporated under Part 1A of the Companies Act of Québec)

CONSOLIDATED BALANCE SHEET
December 31, 1985 (in thousands of dollars)

	1985	1984 (restated note 2)
	$	$
Assets		
CURRENT ASSETS		
Cash and term deposits	**1,980**	1,587
Marketable securities (note 3)	**2,743**	8,110
Bullion at estimated net realizable value	**1,739**	1,550
Accounts receivable	**987**	368
Accrued interest	**36**	88
Supplies at the lower of average cost and replacement value	**896**	610
Prepaid expenses	**67**	30
	8,448	12,343
INVESTMENTS (note 4)	**3,247**	1,476
PROPERTY, PLANT AND EQUIPMENT (note 5)	**22,968**	15,586
DEFERRED CHARGES (note 6)	**1,544**	1,152
	36,207	30,557

ON BEHALF OF THE BOARD OF DIRECTORS

Claude Gauvin

J. Jacques Beauchemin.

Directors

	1985	1984 (restated note 2)
	$	$
Liabilities		
CURRENT LIABILITIES		
Accounts payable and accrued charges	**2,671**	1,272
Mining taxes payable	**83**	42
Dividends payable	**—**	800
Current portion of long-term debt	**400**	213
	3,154	2,327
LONG-TERM DEBT (note 7)	**371**	102
MINORITY INTEREST	**3**	3
SHAREHOLDERS' EQUITY		
CAPITAL STOCK (note 8)	**17,414**	13,303
CONTRIBUTED SURPLUS	**1,459**	1,459
RETAINED EARNINGS	**13,806**	13,363
	32,679	28,125
	36,207	30,557

COMMITMENTS (note 15)

CONTINGENCIES (note 16)

sullivan

CONSOLIDATED EARNINGS

Year ended December 31, 1985 (in thousands of dollars except the amounts per share)

	1985	1984 (restated note 2)
	$	$
Revenue	**10,864**	10,533
Expenses		
Mining operations	**8,384**	6,943
Depreciation and amortization	**1,263**	1,137
	9,647	8,080
MINE OPERATING INCOME	**1,217**	2,453
Other income (Expenses)		
Exploration expenses	**(504)**	(399)
Administration expenses	**(1,062)**	(818)
Interest and dividends	**577**	1,013
Profit on sale of investments	**251**	—
Share in net earnings (loss) of companies subject to significant influence	**47**	(6)
	(691)	(210)
EARNINGS BEFORE UNDERNOTED ITEMS	**526**	2,243
INCOME AND MINING TAXES	**(266)**	(529)
	260	1,714
MINORITY INTEREST	**—**	45
	260	1,759
EXTRAORDINARY ITEMS (note 9)	**183**	(9,278)
NET EARNINGS (LOSS)	**443**	(7,519)
EARNINGS (LOSS) PER SHARE		
Earnings before extraordinary items	**0.03**	0.22
Net earnings (loss)	**0.05**	(0.94)

CONSOLIDATED RETAINED EARNINGS

Year ended December 31, 1985 (in thousands of dollars)

	1985	1984 (restated note 2)
	$	$
BALANCE AT BEGINNING OF YEAR		
As previously reported	**12,742**	21,626
Prior years' adjustments (note 2)	**621**	53
As restated	**13,363**	21,679
NET EARNINGS (LOSS)	**443**	(7,519)
	13,806	14,160
DIVIDENDS	—	797
BALANCE AT END OF YEAR	**13,806**	13,363

CONSOLIDATED CHANGES IN FINANCIAL POSITION

Year ended December 31, 1985 (in thousands of dollars)

	1985	1984 (restated note 2)
	$	$
Operating activities		
Earnings before extraordinary items	**260**	1,760
Items not requiring cash:		
Decrease in current income taxes due to carry over of expenses	**183**	433
Amortization of property, plant and equipment	**1,263**	1,137
Minority interest	—	(45)
Loss on sale of property, plant and equipment	**12**	—
Loss on sale of investment	**51**	—
Share in loss (net earnings) of the companies subject to significant influence	**(47)**	6
	1,722	3,291
Net change in non-cash working capital items	**547**	41
Dividends	**(797)**	(799)
CASH FROM OPERATIONS	**1,472**	2,533
Investing activities		
Additions to property, plant and equipment	**(8,657)**	(3,310)
Acquisition of investments	**(2,240)**	(452)
Sale of investments	**465**	—
Deferred expenses – net	**(393)**	(465)
CASH APPLIED TO INVESTING ACTIVITIES	**(10,825)**	(4,227)
Financing activities		
Long-term debt – net	**456**	315
Issue of common shares	**2,668**	56
Issue of preferred shares	**1,443**	—
CASH FROM FINANCING ACTIVITIES	**4,567**	371
DECREASE IN CASH AND EQUIVALENTS	**(4,786)**	(1,323)
CASH AND EQUIVALENTS, AT BEGINNING OF YEAR	**11,247**	12,570
CASH AND EQUIVALENTS, AT END OF YEAR (note 10)	**6,461**	11,247

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 1985 (Tabular amounts shown in thousands of dollars)

1. Significant accounting policies

BASIS OF PRESENTATION OF FINANCIAL STATEMETNS

The accompanying financial statements are prepared in accordance with accounting principles generally accepted in Canada and are in accordance with International Accounting Standards.

BASIS OF CONSOLIDATION

The accompanying financial statements include, on a consolidated basis, the accounts of Sullivan Mines Inc. (the Company) and all of its subsidiaries.

Courvan Mining Company Limited (No Personal Liability) which was consolidated as at December 31, 1984 is shown at the equity method as at December 31, 1985 because the company reduced its interest from 50.01% to 49.76% by the sale of a number of shares. The 1984 figures have been modified in order to account for the investment at the equity method; the following items have been excluded from the consoldiated statements as at December 31, 1984:

Cash	$ 4,172
Deferred expenses	185,620
Accounts payable	187,233
Minority interest	85,586

These financial statements reflect the proportionate interest that the Company holds in the assets, liabilities, revenue and expenses of several mining and exploration joint ventures.

PROPERTY, PLANT AND EQUIPMENT

Producing assets

(i) Property, plant, buildings and equipment and deferred expenditures are recorded at cost.

(ii) Depreciation on plant, buildings and equipment is provided on the unit-of-production method based on estimated mineral reserves.

(iii) Repairs and maintenance are charged to operations, major betterments and replacements are capitalized.

Non-producing assets

Property, plant and equipment are accounted for as follows:

(i) The Company's share of the assets and liabilities of the Eldrich, Flavel and Croinor Joint Ventures are recorded at cost. Their recovery will only be known once their properties are brought into commercial production at which time the amortization policy will be enunciated by Management.

(ii) Property, plant and equipment used for the office and for exploration are carried at cost. Depreciation is provided using the straight-line method at 15%, 20% per year.

(iii) Property, plant and equipment of the Québec Lithium division are carried at a value that Management considers to be realizable and no depreciation is recorded.

(iv) Mining properties, claims and concessions are valued at cost and at nominal value.

MINERAL EXPLORATION

Exploration expenditures are charged against current earnings unless they relate to properties from which a productive result is reasonably certain or on which work is in progress, in which case they are deferred. Exploration expenditures of Valdez Creek and Dickenson-Sullivan Joint Ventures have been charged to income.

EXCESS OF COST OF INVESTMENT OVER NET ASSETS

Amortization is calculated on the straight-line method over 10 years.

FOREIGN CURRENCY TRANSLATION

Monetary items of assets and liabilities are translated using the rate of exchange at the end of the year and non-monetary items are translated at historical cost. Deferred charges and revenue and expenses other than depreciation are translated by using the average rate for the year. Depreciation is translated at the same rate as the related asset. Profit and loss resulting from these translations are charged or credited to deferred charges.

2. Prior years' adjustments

(i) Change in accounting policies

In 1985, the Company changed the method of calculating the amortization of its interest in the mining properties that it holds in the Valdez Creek Joint Venture from a straight-line basis at 30% per annum to a production basis using total ounces of production per annum. As a result of this change in policy, the investment in mining properties incresed by $300,434 as at December 31, 1984 and retained earnings increased by the same amount. This change resulted in an increase of 1985 earnings by $495,741.

(ii) Prior years' adjustment

This adjustment is the result of the recovery of Ontario Mining taxes amounting to $321,288 being $267,860 for the year 1984 and $53,428 for 1983, net earnings for 1984 have been increased by $267,860 while mining taxes payable at December 31, 1984 have been decreased by $321,288.

3. Marketable securities, at cost

	1985	1984
	$	$
Deposit notes	743	4,663
Bonds (market value, 1985, $2,000,000; 1984, $3,003,750)	2,000	3,000
Shares (market value, 1984, $478,060)	—	447
	2,743	8,110

4. Investments, at cost

	1985	1984
	$	$
Shares of exploration companies		
Accounted for on the equity basis:		
1,500,006 common shares of Goldquest Explorations Inc. (1984 at cost) representing 22.299% of the shares with voting rights (1984, 472,637 shares) (Market value, 1985, $1,545,004; 1984 , $519,900)	1,585	514
The excess of cost over net assets acquired amounts to $204,204. As at December 31, 1985, the unamortized amount of goodwill included by the equity method is $195,696.		
1,990,500 common shares of Courvan Mining Company Limited (No Personal Liability) (1984 consolidated subsidiary) representing 49.76% of shares with voting rights, (1984, 2,000,500) (market value 1985, $696,675; 1984, $700,175)	149	86
Other shares, at cost (market value 1985, $135,333; 1984, $590,100)	350	866
	2,084	1,466
Other securities		
Government of Canada coupons with accrued interest thereon of $52,443 (market value, $959,580) deposited as guarantee, see below	931	—
Loan to an officer – employee	25	—
Advance to a related company, without interest and with no fixed term of reimbursement	207	10
	3,247	1,476

The company has deposited with the Guaranty Trust Company of Canada a sufficient amount which at maturity will provide for the redemption of the Series A preferred shares. The Company will be allowed to reduce this deposit upon the conversion of preferred shares into common shares (note 8).

5. Property, plant and equipment

	1985	1984
	$	$
Producing assets		
Dickenson-Sullivan Joint Venture at cost:		
Buildings, equipment, deferred development and mining claims . .	**11,977**	11,380
Less: Accumulated depreciation	**3,146**	2,194
	8,831	9,186
Valdez Creek Joint Venture at cost:		
Buildings, equipment, deferred development and mining claims . .	**4,269**	1,526
Less: Accumulated depreciation	**409**	160
	3,860	1,366
Total producing assets	**12,691**	10,552
Non-producing assets		
Eldrich Joint Venture, at cost	**5,016**	1,495
Flavel Joint Venture, at cost	**1,696**	—
Croinor Joint Venture, at cost	**2,366**	2,345
Mining properties, claims and concessions at cost and at nominal value	**155**	155
Buildings, machinery and equipment		
– at cost less accumulated depreciation of $166,115 (1984, $121,263)	**281**	276
– at estimated realizable value	**763**	763
Total non-producing assets	**10,277**	5,034
Total	**22,968**	15,586

6. Deferred charges

	1985	1984
	$	$
These charges represent the cost of projects at the mineral exploration stage		
Accumulated balance at beginning of year	**1,151**	2,918
Additions during the year	**511**	1,043
	1,662	3,961
Less:		
Transfers to costs of Joint Ventures	**—**	2,582
Expenses of terminated projects	**118**	227
	118	2,809
Accumulated at end of year	**1,544**	1,152

7. Long-term debt

	1985	1984
	$	$
Notes payable, maturing May 3, 1987, bearing interest at 1.50% above a chartered bank's prime rate, with the principal repayable in equal monthly instalments of $8,570 plus interest	**154**	126
Note payable, maturing December 15, 1987, bearing interest at 13%, with the principal repayable in equal monthly instalments of $28,759 including interest, from June to December of each year and $289,287 of unpaid instalments due in 1985	**363**	—
Mining claim payments	**50**	39
Obligations under capital leases, interest imputed at 1.125% on a monthly basis maturing in 1986	**204**	150
	771	315
Portion included in current liabilities	**400**	213
	371	102

The note payable is collateralized by certain machinery and equipment having a book value of $1,150,194. Interest related to long-term debt excluding the interest portion of payments made on equipment acquired under capital leases amounted to approximately $79,428 in 1985.

8. Capital stock

	Shares	1985	1984
		$	$
AUTHORIZED			
An unlimited number of preferred shares without par value, which can be issued in one of several Series, with rights, privileges, restrictions and conditions as determined by the Board of Directors.			
An unlimited number of common shares without par value.			
ISSUED AND PAID			
222,000 preferred shares, Series A issued on August 15, 1985. These shares are issued by virtue of agreements of Société en Commandite Sullivan (a limited partnership) and are accounted for at the cost at which they can be redeemed	222,000	**1,443**	—
Common shares (see subsequent event note 18)			
Issued at beginning of year	7,999,029	**13,303**	13,303
Issued during year private placement for cash	284,240	**2,668**	—
	8,283,269	**15,971**	13,303
TOTAL		**17,414**	13,303

PREFERRED SHARES, SERIES A

These preferred shares are non-voting and non-participating, are convertible into one common share of the Company after August 15, 1986 and until June 30, 1990 and are redeemable at the option of the holder on September 17, 1990 for an amount of $6.50 per share or at the option of the Company for an amount of $12.41 after June 30, 1990. These shares can be redeemed by the Company following an offer by the Company and accepted by the holders of the preferred shares.

On dissolution of the Company or on the distribution of its assets to its shareholders, the holders of Series A preferred shares will be entitled to receive an amount of $12.41 for each share held, before any distribution to the common shareholders.

COMMON SHARES UNDER OPTION TO EMPLOYEES

The Company has granted options to its permanent employees including six (6) senior executives, on 106,300 shares of its capital stock at a price of $4.00 and $5.00 per share for a period of three (3) years ending on January 14, 1986. A total of 69,500 were subscribed up to December 31, 1985 (1984, 69,500), 7,400 were cancelled during 1985 leaving a balance of 29,400 shares under option.

During the year, the Company granted an option to a senior executive on 40,000 common shares of its capital stock at a price of $3.52 per share for a period of 5 years.

9. Extraordinary items

	1985	1984
	$	$
Reduction of income taxes due to a carry-over of expenses	**183**	433
Write-off of contribution by the subsidiary, Brunswick Tin Mines Limited (No Personal Liability) to Mount Pleasant Tungsten Mine Joint Venture	**—**	(9,711)
	183	(9,278)

10. Cash and equivalents

	1985	1984
	$	$
The cash and equivalents consist of:		
Cash and term deposits	**1,980**	1,587
Marketable securities	**2,743**	8,110
Bullion	**1,738**	1,550
	6,461	11,247

11. SOQUEM

Under the terms of an agreement dated February 27, 1981 whereby SOQUEM acquired 1,500,000 shares of the Company, it was provided that during a seven (7) year exploration period, Sullivan would not declare and pay any dividends, unless sufficient operating profits from all sources, including investment income, excepting the income derived from the proceeds of the SOQUEM subscription, that would cover the total dividends declared and paid. The dividends declared and paid in 1984 meet with this condition.

12. Joint Ventures

The following amounts represent the Company's interest in the following Joint Ventures which are accounted for by the proportionate consolidation method, Dickenson-Sullivan, Valdez Creek, Eldrich, Flavel and Croinor. The first two are operating mines while the last three are at the exploration stage.

	1985	1984
Assets	**21,040**	13,148
Liabilities	**2,764**	1,693
Revenue	**10,864**	10,533
Expenses	**8,384**	6,943

13. Timing differences

The financial statements do not reflect debit deferred income taxes on timing differences. These timing differences of $31,798,000 are available for an indefinite period.

14. Government assistance

The Company was granted financial assistance by the Government of the Province of Quebec in order to accelerate the exploration of the Eldrich-Flavel project and to reach the production stage. The maximum amount of the assistance granted to Sullivan Mines Inc. is $4.5 million, for the joint benefit of the participants and covers two phases estimated to cost $28 million. As at December 31, 1985, the Company received $1,513,000 which reduced the Company's expenditures.

The total cost of phase 1 of the project amounted to more than the anticipated costs of $10,654,000 as at December 31, 1985. The work will continue during the first quarter of 1986 in order to complete the development programme. Should the Company abandon the project it will have to reimburse to the Government all sums received without interest.

15. Commitments

(i) The minimum payments relating to operating leases expiring from April 30, 1986 to April 30, 1992 total $479,162. The payments required over the next five years are as follows: 1986, $92,759; 1987, $82,053; 1988, $70,176; 1989, $70,238 and 1990, $70,238.

(ii) By virtue of the terms of an agreement and in consideration of services rendered, the Company has agreed to pay, to a retiring officer, an amount of $30,000 per year, for a period of four years ending on December 31, 1986.

(iii) The Dickenson-Sullivan Joint Venture, through its joint venturers, Dickenson Mines Limited and Sullivan Resources Ltd. has guaranteed apartment leases for use by employees at the Arthur W. White Mine for $547,000 per year from 1986 to 1989 and $561,000 plus financing adjustments, if any, from 1990 to 1995.

16. Contingency

LEGAL PROCEEDINGS

(i) Legal proceedings have been instituted against the Company and its Agents by the Owners of a vessel for an accident which occurred during the shipment of concentrates. This claim is being contested by the Company. The amount of the possible liability cannot be determined at this time bacause the Company and its agent have exercised a recourse seeking indemnity from a third party.

However, the Company has issued a guarantee in the amount of $200,000 U.S. as security for the payment of any judgement that might be rendered in favour of the Owners of the vessel. A sum of $98,000 has been provided for in the books. Should any judgement be rendered against the Company and if the amount exceeds the sum provided for in the books, the excess will be accounted for as an adjustment of prior years.

(ii) An action was commenced by Mount Pleasant Resources Inc. against Billiton Canada Limited, Billiton Metals Canada Inc. and Brunswick Tin Mines Limited.

As against Brunswick Tin Mines Limited, the claim is for an accounting and damages in the amount of $10,000,000 in respect of a letter agreement between Mount Pleasant Resources Inc. and Brunswick Tin Mines Limited.

A third party claim is being made against Lac Minerals Ltd. and a crossclaiming against Billiton Canada Limited and Billiton Metals Canada Inc. for indemnity.

In the opinion of the solicitors of Brunswick Tin Mines Limited the latter should have no liability in the circumstances.

17. Mount Pleasant Tungsten Mine (Joint Venture)

CESSATION OF EXPLOITATION OF THE PROPERTY

On May 16, 1985, Billiton advised Brunswick that it had decided to cease exploitation of the property because there was a negative cashflow, and in view of high operating cost and continued depressed prices there appeared to be no likelihood of a positive cashflow in the foreseeable future sufficient to allow repayment of all monies advanced under the Agreement and the Loan Agreement plus interest thereon. Following the cessation of exploitation Billiton Canada Limited proceeded to liquidate the assets which gave rise to the court action mentioned in note 16.

18. Subsequent event

Pursuant to private placement agreements entered into on December 31, 1985, the Company reserved for issuance 150,000 common shares at $10.00 per share for a total consideration of $1,500,000. These funds are to be used to incur Canadian Exploration Expenses for the benefit of the investors and are held In Trust until February 28, 1986.

19. Comparative figures

The presentation of certain accounts of the previous year has been changed to conform with the presentation adopted for the current year.

AUDITORS' REPORT

To the Shareholders of
Sullivan Mines Inc.

We have examined the consolidated balance sheet of Sullivan Mines Inc. as at December 31, 1985 and the consolidated statements of earnings, retained earnings and changes in financial position for the year then ended and we have obtained all the information and explanations we have required. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, according to the best of our information and explanations given to us and as shown by the books of the company, these consolidated financial statements present fairly the financial position of the company as at December 31, 1985 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied, after giving retroactive effect to the change in the method of amortizing the investment in mining properties as explained in note 2 to the financial statements, on a basis consistent with that of the preceding year.

Maheu Noiseux
Chartered Accountants

Montreal, February 20, 1986

Sullivan Mines Inc.

Board of Directors

J. Jacques Beauchemin, Q.C.
Lucien C. Béliveau, Eng.
Paul J. Bourassa, Eng.
William G. Brissenden, Eng.
Jean-Paul Drolet, Eng.
Georges Gauvreau, Notary
Claude Genest, L.S.C.
Réal J. Lafleur
André Latreille, Eng.
Alexandre J. Montminy

Officers

J. Jacques Beauchemin, Q.C.
Chairman of the Board

Lucien C. Béliveau, Eng.
Vice-Chairman of the Board

Claude Genest, L.S.C.
President and Chief Executive Officer

Réal J. Lafleur
Vice-President Finance and Secretary-Treasurer

Jean Depatie, M.Sc., Geologist
Vice-President Exploration

Daniel Goffaux, Eng.
General Manager, Eldrich-Flavel Project

Linda Caty, Lawyer
Assistant Secretary

Alain Taillefer, C.A., R.I.A.
Assistant Comptroller

Earl Quon
Chief Accountant

Boards of Directors of Subsidiaries and Affiliated Companies

Sullivan Resources Ltd

Claude Genest, *President*
Lucien C. Béliveau
William G. Brissenden
Jean-Paul Drolet
Réal J. Lafleur
André Latreille

FEDPEN Ltée

Claude Genest, *President*
Lucien C. Béliveau
François J. Bastien
Georges Gauvreau
Réal J. Lafleur
André Latreille

Brunswick Tin Mines Limited

Claude Genest, *President*
Lucien C. Béliveau
Jean-Paul Drolet
André Latreille
Andrew Stein
Keith Stein

Courvan Mining Company Limited

Claude Genest, *President*
Lucien C. Béliveau
François G. Bastien, C.A.
Jean Depatie
Georges Gauvreau
André Latreille

SUM Resources Inc.

Claude Genest, *President*
Lucien C. Béliveau
Jean-Paul Drolet

Various Committees

Finance

Claude Genest
Réal J. Lafleur
André Latreille

Compensation

Lucien C. Béliveau
William G. Brissenden
Georges Gauvreau

Audit

J. Jacques Beauchemin
Jean-Paul Drolet
André Latreille

Gold in 1985

According to data compiled by the Department of Energy, Mines and Resources, the price of gold has been declining for the third consecutive year. It averaged a little over $317 US an ounce ($433 Cdn) in 1985, compared with $360 US ($467 Cdn) in 1984 and $424 US ($523 Cdn) in 1983.

Gold hit a low of around $285 US during the month of February 1985, while a high of $340 US was reached in August. The average price during the final quarter of 1985 was $324 US.

Total Canadian gold production for 1985 was over 86,000 kilograms (equivalent to 2,765,000 troy ounces), which represented an increase of 3% over the preceding year. Ontario ranked first among gold producers with some 31,670 Kgs, (well over 1 million ounces), followed by Quebec (29,303 Kgs) and the Northwest Territories (12,980 Kgs).

Gold production is expected to increase in coming years, particularly in Quebec and Ontario. Considering the present level of exploration and development, several new gold deposits will probably come into production if the gold price remains at a respectable level. According to gold specialists, the price should vary between $310 US and $360 US during 1986.

Despite falling prices, gold production has increased slightly, price level being still above the average production cost. Another factor has been the declining value of the Canadian dollar in relation to the American dollar.

GOLD PRICES – 1985

LONDON GOLD MARKET – AM FIX

Weight equivalent: 1 kilogram = 32.15 troy ounces.

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