

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

☒ ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended September 30, 2010

OR

☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

Commission file number: 001-34055



TIMBERLINE RESOURCES CORPORATION

(Exact Name of Registrant as Specified in its Charter)

Delaware

82-0291227

(State of other jurisdiction of incorporation or organization)

(I.R.S. Employer Identification No.)

101 East Lakeside Avenue

Coeur d'Alene, Idaho

83814

(Address of Principal Executive Offices)

(Zip Code)

(208) 664-4859

(Registrant's Telephone Number, including Area Code)

SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT:

Title of Each Class

Name of Each Exchange on Which Registered

Common Stock, \$0.001 par value

NYSE Amex

TSX Venture Exchange

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT: **None**

Indicate by check mark if the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☐ No ☒

Indicate by check mark if the Registrant is not required to file reports pursuant to Section 13 or 15(d) of the Exchange Act. ☐

Indicate by check mark whether the Registrant (1) has filed all reports required by Section 13 or 15(d) of the Securities Exchange Act of 1934 ("Exchange Act") during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark whether the Registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 229.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☐ No ☐

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definition of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ☐

Accelerated filer ☐

Non-accelerated filer ☐

Smaller reporting company ☒

Indicate by check mark whether the Registrant is a shell company, as defined in Rule 12b-2 of the Exchange Act. Yes ☐ No ☒

As of March 31, 2010, the aggregate market value of the 41,244,398 shares of Common Stock of the registrant issued and outstanding on such date, which excludes 6,429,162 shares held by affiliates of the registrant as a group, was \$36,555,998. This figure is based on the closing sale price of \$1.05 per share of the Registrant's Common Stock on March 31, 2010 on the NYSE Amex.

Number of shares of Common Stock outstanding as of December 15, 2010: 55,792,938

Documents incorporated by reference: To the extent herein specifically referenced in Part III, portions of the Registrant's definitive Proxy Statement for the 2010 Annual General Meeting of Shareholders. See Part III.

TABLE OF CONTENTS

CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS	1
PART I	2
ITEM 1. DESCRIPTION OF BUSINESS	2
ITEM 1A. RISK FACTORS AND UNCERTAINTIES	5
ITEM 1B. UNRESOLVED STAFF COMMENTS	11
ITEM 2. DESCRIPTION OF PROPERTIES	12
ITEM 3. LEGAL PROCEEDINGS	27
ITEM 4. [REMOVED AND RESERVED]	27
PART II	28
ITEM 5. MARKET FOR COMMON EQUITY, RELATED STOCKHOLDER MATTERS, AND ISSUER PURCHASES OF EQUITY SECURITIES	28
ITEM 6. SELECTED FINANCIAL DATA	29
ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATION	29
ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK	35
ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA	36
ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE	65
ITEM 9A. CONTROLS AND PROCEDURES	65
ITEM 9B. OTHER INFORMATION	65
PART III	66
ITEM 10. DIRECTORS, EXECUTIVE OFFICERS, AND CORPORATE GOVERNANCE	66
ITEM 11. EXECUTIVE COMPENSATION	66
ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDERS MATTERS	66
ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS AND DIRECTOR INDEPENDENCE	66
ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES	66
PART IV	66
ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES	66
SIGNATURES	68

CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K and the exhibits attached hereto contain “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995, as amended. Such forward-looking statements concern the Company’s anticipated results and developments in the Company’s operations in future periods, planned exploration and development of its properties, plans related to its business and other matters that may occur in the future. These statements relate to analyses and other information that are based on forecasts of future results, estimates of amounts not yet determinable and assumptions of management.

Any statements that express or involve discussions with respect to predictions, expectations, beliefs, plans, projections, objectives, assumptions or future events or performance (often, but not always, using words or phrases such as “expects” or “does not expect”, “is expected”, “anticipates” or “does not anticipate”, “plans”, “estimates” or “intends”, or stating that certain actions, events or results “may”, “could”, “would”, “might” or “will” be taken, occur or be achieved) are not statements of historical fact and may be forward-looking statements. Forward-looking statements are subject to a variety of known and unknown risks, uncertainties and other factors which could cause actual events or results to differ from those expressed or implied by the forward-looking statements, including, without limitation:

- risks related to our properties being in the exploration stage;
- risks related our mineral operations being subject to government regulation;
- risks related to our ability to obtain additional capital to develop our resources, if any;
- risks related to mineral exploration and development activities;
- risks related to mineral estimates;
- risks related to our insurance coverage for operating risks;
- risks related to the fluctuation of prices for precious and base metals, such as gold, silver and copper;
- risks related to the competitive industry of mineral exploration;
- risks related to our title and rights in our mineral properties;
- risks related to our limited operating history;
- risks related the possible dilution of our common stock from additional financing activities;
- risks related to potential conflicts of interest with our management;
- risks related to our subsidiaries’ activities; and
- risks related to our shares of common stock.

This list is not exhaustive of the factors that may affect our forward-looking statements. Some of the important risks and uncertainties that could affect forward-looking statements are described further under the sections titled “Risk Factors and Uncertainties”, “Description of Business” and “Management’s Discussion and Analysis” of this Annual Report. Should one or more of these risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual results may vary materially from those anticipated, believed, estimated or expected. We caution readers not to place undue reliance on any such forward-looking statements, which speak only as of the date made. We disclaim any obligation subsequently to revise any forward-looking statements to reflect events or circumstances after the date of such statements or to reflect the occurrence of anticipated or unanticipated events, except as required by law.

We qualify all the forward-looking statements contained in this Annual Report by the foregoing cautionary statements.

PART I

ITEM 1. DESCRIPTION OF BUSINESS

General

We were incorporated in the State of Idaho on August 28, 1968 under the name Silver Crystal Mines, Inc., to engage in the business of exploring for precious metal deposits and advancing them toward production. We ceased exploration activities during the 1990s and became virtually inactive. In December 2003, a group of investors purchased 80-percent of the issued and outstanding common stock from the then-controlling management team. In January 2004, we effected a one-for-four reverse split of our issued and outstanding shares of common stock and increased the number of our authorized shares of common stock to 100 million with a par value of \$.001. Unless otherwise indicated, all references herein to shares outstanding and share issuances have been adjusted to give effect to the aforementioned stock split. On February 2, 2004, our name was changed to Timberline Resources Corporation. Since the reorganization, we have been in an exploration stage evaluating, acquiring and exploring mineral prospects with potential for economic deposits of precious and base metals. A prospect is defined as a mining property, the value of which has not been determined by exploration. On August 27, 2008 we reincorporated into the State of Delaware pursuant to a merger agreement approved by our shareholders on August 22, 2008.

In March 2006, we acquired Timberline Drilling, Inc. (“Timberline Drilling”), formerly known as Kettle Drilling, as a wholly-owned subsidiary. Timberline Drilling was formed in 1996 and provides mineral core drilling services to the mining and mineral exploration industries primarily in the western United States.

In July 2007, we closed our purchase of the Butte Highlands Gold Project. In October 2008, we announced that we had agreed to form a 50/50 joint venture with Small Mine Development (“SMD”) at the Butte Highlands project. In July 2009, we finalized the joint venture agreement with Highland Mining, LLC (an affiliate of SMD) (“Highland”) to create Butte Highlands JV, LLC (“BHJV”). Under terms of the joint venture agreement, Timberline will be carried to production by Highland, which will fund all mine development costs and began development in the summer of 2009. Both Timberline’s and Highland’s 50-percent share of costs will be paid out of net proceeds from future mine production.

In June 2010, we closed our acquisition of Staccato Gold Resources Ltd., a Canadian-based resource company (“Staccato Gold”) that was in the business of acquiring, exploring and developing mineral properties with a focus on gold exploration in the dominant gold producing trends in Nevada. As a result of this acquisition, we obtained Staccato’s flagship gold exploration project (“Lookout Mountain”), and several other projects at various stages of exploration in the Battle Mountain/Eureka gold trend in north-central Nevada, along with Staccato Gold’s wholly owned U.S. subsidiary, BH Minerals USA, Inc.

In September 2010, we closed our drilling services operation in Mexico which was operated by our wholly owned Mexican subsidiary, World Wide Exploration, S.A. de C.V. (“World Wide” or “WWE”), and moved substantially all of the assets of WWE to the United States to be available for use by Timberline Drilling.

Unless otherwise indicated, any reference to “Timberline”, or “we”, “us”, “our”, etc. refers to Timberline Resources Corporation and/or all its subsidiaries, including Timberline Drilling and Staccato Gold.

Our Competition

Both the mineral exploration and drilling industries are intensely competitive in all phases. In our mineral exploration activities, we will compete with many companies possessing greater financial resources and technical facilities than us for the acquisition of mineral concessions, claims, leases and other mineral interests as well as for the recruitment and retention of qualified employees. We must overcome significant barriers to enter into the business of mineral exploration as a result of our limited operating history.

Similarly, in our drilling business, our competition includes many companies with significantly greater experience, larger client bases, and substantially greater financial resources. There are significant barriers to entry including large capital requirements and the recruitment and retention of qualified, experienced employees.

We cannot assure you that we will be able to compete in any of our business areas effectively with current or future competitors or that the competitive pressures faced by us will not have a material adverse effect on our business, financial condition and operating results.

Our Offices and Other Facilities

Timberline currently maintains its administrative office at 101 East Lakeside Ave., Coeur d’Alene, ID 83814. The telephone number is (866) 513-4859 (toll free) or (208) 664-4859. Timberline also maintains a geological staff office at 1112 River St., Elko, NV 89801. Timberline Drilling maintains its administrative office at 2775 Howard Street, Suite 2, Coeur d’Alene, ID 83815. Timberline Drilling’s telephone number is 208-665-7211. In addition, Timberline Drilling maintains a shop facility in Coeur d’Alene, ID and an operational facility in Elko, NV.

Our Employees

Timberline, the parent company, is an exploration company and currently has six employees, including certain officers and directors. Management expects to hire staff and additional management as necessary as implementation of our business plan requires.

Our subsidiary, Timberline Drilling, has approximately 130 full-time employees in the U.S. Our Staccato Gold subsidiary does not have any employees. We believe that our relationship with our employees is good.

Regulation

The exploration, drilling and mining industries operate in a legal environment that requires permits to conduct virtually all operations. Thus permits are required by local, state and federal government agencies. Federal agencies that may be involved include: The U.S. Forest Service (USFS), Bureau of Land Management (BLM), Environmental Protection Agency (EPA), National Institute for Occupational Safety and Health (NIOSH), the Mine Safety and Health Administration (MSHA) and the Fish and Wildlife Service (FWS). Individual states also have various environmental regulatory bodies, such as Departments of Ecology and so on. Local authorities, usually counties, also have control over mining activity. The various permits address such issues as prospecting, development, production, labor standards, taxes, occupational health and safety, toxic substances, air quality, water use, water discharge, water quality, noise, dust, wildlife impacts, as well as other environmental and socioeconomic issues.

Prior to receiving the necessary permits to explore or mine, the operator must comply with all regulatory requirements imposed by all governmental authorities having jurisdiction over the project area. Very often, in order to obtain the requisite permits, the operator must have its land reclamation, restoration or replacement plans pre-approved. Specifically, the operator must present its plan as to how it intends to restore or replace the affected area. Often all or any of these requirements can cause delays or involve costly studies or alterations of the proposed activity or time frame of operations, in order to mitigate impacts. All of these factors make it more difficult and costly to operate and have a negative and sometimes fatal impact on the viability of the exploration or mining operation. Finally, it is possible that future changes in these laws or regulations could have a significant impact on our business, causing those activities to be economically reevaluated at that time. For a more detailed discussion of governmental and environmental regulatory requirements applicable to our mineral exploration business see the section titled "Description of Properties - Overview of Regulatory, Economic and Environmental Issues" below.

Overview of Our Mineral Exploration Business

Timberline, the parent company, is a mineral exploration company. Mineral exploration is essentially a research activity that does not produce a product. Successful exploration often results in increased project value that can be realized through the optioning or selling of the claimed site to larger companies. As such, we acquire properties which we believe have potential to host economic concentrations of minerals, particularly gold, silver and copper. These acquisitions have and may take the form of unpatented mining claims on federal land, or leasing claims, or private property owned by others. An unpatented mining claim is an interest that can be acquired to the mineral rights on open lands of the federally owned public domain. Claims are staked in accordance with the Mining Law of 1872, recorded with the federal government pursuant to laws and regulations established by the Bureau of Land Management (the Federal agency that administers America's public lands), and grant the holder of the claim a possessory interest in the mineral rights, subject to the paramount title of the United States.

We will perform basic geological work to identify specific drill targets on the properties, and then collect subsurface samples by drilling to confirm the presence of mineralization (the presence of economic minerals in a specific area or geological formation). We may enter into joint venture agreements with other companies to fund further exploration work. It is our plan to focus on assembling a high quality group of mid-stage mineral (gold, silver, and copper) exploration prospects, using the experience and contacts of the management group. By such prospects, we mean properties that may have been previously identified by third parties, including prior owners such as exploration companies, as mineral prospects with potential for economic mineralization. Often these properties have been sampled, mapped and sometimes drilled, usually with indefinite results. Accordingly, such acquired projects will either have some prior exploration history or will have strong similarity to a recognized geologic ore deposit model. Geographic emphasis will be placed on the western United States.

The focus of our activity has been to acquire properties that we believe to be undervalued; including those that we believe to hold previously unrecognized mineral potential. Properties have been acquired through the location of unpatented mining claims (which allow the claimholder the right to mine the minerals without holding title to the property), or by negotiating lease/option agreements. Our Executive Chairman and Vice-President of Exploration, Paul Dirksen, has experience in evaluating, staking and filing unpatented mining claims, and in negotiating and preparing mineral lease agreements in connection with those mining claims.

The geologic potential and ore deposit models have been defined and specific drill targets identified on the majority of our properties. Our property evaluation process involves using basic geologic fieldwork to perform an initial evaluation of a property. If the evaluation is positive, we seek to acquire it, either by staking unpatented mining claims on open public domain, or by leasing the property from the owner of private property or the owner of unpatented claims. Once acquired, we then typically make a more detailed evaluation of the property. This detailed evaluation involves expenditures for exploration work which may include rock and soil sampling, geologic mapping, geophysics, trenching, drilling, or other means to determine if economic mineralization is present on the property.

[TABLE OF CONTENTS](#)

Portions of our mineral properties are owned by third parties, and leased to us, as outlined in the following table.

Property Name	Third Party	Number of Claims	Area	Agreements/Royalties
Butte Highlands	Richardson Family Trust	4	60 acres	3% to 4% NSR; Annual lease payment of \$15,000 through 2012 and \$20,000 each year thereafter on October 1. Option to purchase property during lease term for \$2,000,000.
Snowstorm	Hecla Mining Company	38	750 acres	4% NSR
Snowstorm	Snowshoe Mining Company	6	78 acres	3% NSR
Spencer	Idaho, Department of Lands	Section 6, T12N R36E	640 acres	5% NSR
Lookout Mountain	Rocky Canyon Mining Company	373	6,368 acres	3.5% NSR royalty + 1.5% NSR royalty capped at \$1.5 million (excludes Trevor and Dave claims); 20 year lease term commencing June 1, 2008; annual advanced royalty payment of \$72,000. (Pending legal opinion, additional 2% NSR possible)
Windfall Patents	Century Gold	13	166 acres	Annual lease payment of \$48,000; April 1, 2012 lease term; property may be purchased anytime before February 28, 2012 for \$750,000; 4% NSR

All of the leases are contracts with varied terms, all of which provide for us to earn an interest in the property or receive a royalty. For additional information see “Description of Property” below.

Our strategy with properties deemed to be of higher risk or those that would require very large exploration expenditures is to present them to larger companies for joint venture. Our joint venture strategy is intended to maximize the abilities and skills of the management group, conserve capital, and provide superior leverage for investors. If we present a property to a major company and they are not interested, we will continue to seek an interested partner.

For our prospects where drilling costs are reasonable and the likelihood of success seems favorable, we will undertake our own drilling. The target depths, the tenor of mineralization on the surface, and the general geology of the area are all factors that determine the risk as calculated by us in conducting a drilling operation. Mineral exploration is a research and development activity and is, by definition, a high risk business that relies on numerous untested assumptions and variables. Accordingly, we make our decisions on a project by project basis. We do not have any steadfast formula that we apply in determining the reasonableness of drilling costs in comparison to the likelihood of success, i.e. in determining whether success seems “favorable.”

Overview of Timberline Drilling, Incorporated – Our Wholly Owned Subsidiary

In March 2006, Timberline acquired Kettle Drilling, Inc., which in September 2008 changed its name to Timberline Drilling, Inc. Timberline Drilling provides core drilling services to mining and mineral exploration companies, primarily in the western United States, combining state of the art equipment, world-class technical expertise, innovative thinking, and a strong safety record. Timberline Drilling specializes in underground drilling services in support of active mining operations and advanced exploration projects. Working primarily with established companies, its business is less cyclical than that of surface drillers at early-stage exploration sites, where supplies, infrastructure, and project funding are less predictable.

Timberline Drilling has a fleet of 25 drill rigs which generated revenues of approximately \$6.6 million in the quarter ending September 30, 2010, raising overall revenue for the 2010 fiscal year to more than \$20.7 million, excluding revenue generated by drilling for Timberline Resources in Nevada and Montana.

TABLE OF CONTENTS

During the year ended September 30, 2010, due to a difficult operating environment, declining financial results, and increasing country-related risk, we decided to cease the operations of Timberline Drilling's wholly-owned Mexican subsidiary, World Wide. World Wide's drill rigs and related assets were moved back to the U.S. where they will be available for use by Timberline Drilling.

Looking ahead to the 2011 fiscal year, the ongoing general economic uncertainty continues to affect the ability of some of our potential clients to raise funds for drilling programs. Our underground drilling operations in support of operating mines continue to perform well in the U.S., and we have seen some increase in requests for surface drilling services as well. Revenues, gross profit and net income at Timberline Drilling increased considerably in comparison to the prior fiscal year, and we expect our revenues and profits to remain somewhat stable for the foreseeable future, with a potential for modest growth should drilling activity increase and commodity prices remain at or near current levels. We also expect to continue to improve our cash flows as management focuses on profitability and customer service at Timberline Drilling. See "Management's Discussion and Analysis of Financial Condition and Results of Operations" below.

The Commodities Market

The prices of gold and silver have fluctuated during the last several years, although the price of gold has risen steadily over the past year. In 2008, gold traded between approximately \$690 and \$1,025 per ounce, based on the London PM Fix Price. In 2009, gold traded between approximately \$810 and \$1,212, and in 2010 to date, gold has traded between approximately \$1,058 and \$1,421 (based on the London PM Fix Price). The price of gold based on the London PM Fix Price closed at \$1,389 on December 15, 2010.

In 2008, the price of silver per ounce ranged from approximately \$8.80 to \$20.90, based on the London Fix Price. In 2009, the price of silver ranged from approximately \$10.50 to \$19.18 per ounce, and in 2010 to date, silver has traded between approximately \$15.14 and \$30.50 (based on the London Fix Price). The price of silver based on the London Fix Price closed at \$29.06 on December 15, 2010.

Seasonality

Seasonality in Nevada and Montana is not a material factor to our operations. Certain surface exploration work may need to be conducted when there is no snow on the ground but it is not a material issue.

ITEM 1A. RISK FACTORS AND UNCERTAINTIES

An investment in a mine service and an exploration stage mining company with a short history of operations such as ours involves an unusually high amount of risk, both known and unknown, present and potential, including, but not limited to the risks enumerated below.

Failure to successfully address the risks and uncertainties described below would have a material adverse effect on our business, financial condition and/or results of operations, and the trading price of our common stock may decline and investors may lose all or part of their investment. We cannot assure you that we will successfully address these risks or other unknown risks that may affect our business.

Estimates of mineralized material are forward-looking statements inherently subject to error. Although resource estimates require a high degree of assurance in the underlying data when the estimates are made, unforeseen events and uncontrollable factors can have significant adverse or positive impacts on the estimates. Actual results will inherently differ from estimates. The unforeseen events and uncontrollable factors include: geologic uncertainties including inherent sample variability, metal price fluctuations, variations in mining and processing parameters, and adverse changes in environmental or mining laws and regulations. The timing and effects of variances from estimated values cannot be accurately predicted.

Risks Associated With Mining and the Exploration Portion of Our Business

All of our properties are in the exploration or development stage. There is no assurance that we can establish the existence of any mineral reserve on any of our properties in commercially exploitable quantities. Until we can do so, we cannot earn any revenues from these properties and if we do not do so we will lose all of the funds that we expend on exploration. If we do not discover any mineral reserve in a commercially exploitable quantity, the exploration component of our business could fail.

We have not established that any of our mineral properties contain any mineral reserve according to recognized reserve guidelines, nor can there be any assurance that we will be able to do so. A mineral reserve is defined by the Securities and Exchange Commission in its Industry Guide 7 (<http://www.sec.gov/divisions/corpfin/forms/industry.htm#secguide7>) as that part of a mineral deposit, which could be economically and legally extracted or produced at the time of the reserve determination. The probability of an individual prospect ever having a "reserve" that meets the requirements of the Securities and Exchange Commission's Industry Guide 7 is extremely remote; in all probability our mineral property does not contain any 'reserve' and any funds that we spend on exploration will probably be lost. Even if we do eventually discover a mineral reserve on one or more of our properties, there can be no assurance that they can be developed into producing mines and extract those minerals. Both mineral exploration and development involve a high degree of risk and few properties which are explored are ultimately developed into producing mines.

The commercial viability of an established mineral deposit will depend on a number of factors including, by way of example, the size, grade and other attributes of the mineral deposit, the proximity of the mineral deposit to infrastructure such as a smelter, roads and a point for shipping, government regulation and market prices. Most of these factors will be beyond our control, and any of them could increase costs and make extraction of any identified mineral deposit unprofitable.

Mineral operations are subject to applicable law and government regulation. Even if we discover a mineral reserve in a commercially exploitable quantity, these laws and regulations could restrict or prohibit the exploitation of that mineral reserve. If we cannot exploit any mineral reserve that we might discover on our properties, our business may fail.

Both mineral exploration and extraction require permits from various foreign, federal, state, provincial and local governmental authorities and are governed by laws and regulations, including those with respect to prospecting, mine development, mineral production, transport, export, taxation, labor standards, occupational health, waste disposal, toxic substances, land use, environmental protection, mine safety and other matters. Regarding our future ground disturbing activity on federal land, we will be required to obtain a permit from the US Forest Service or the Bureau of Land Management prior to commencing exploration. There can be no assurance that we will be able to obtain or maintain any of the permits required for the continued exploration of our mineral properties or for the construction and operation of a mine on our properties at economically viable costs. If we cannot accomplish these objectives, our business could face difficulty and/or fail.

We believe that we are in compliance with all material laws and regulations that currently apply to our activities but there can be no assurance that we can continue to do so. Current laws and regulations could be amended and we might not be able to comply with them, as amended. Further, there can be no assurance that we will be able to obtain or maintain all permits necessary for our future operations, or that we will be able to obtain them on reasonable terms. To the extent such approvals are required and are not obtained, we may be delayed or prohibited from proceeding with planned exploration or development of our mineral properties.

Environmental hazards unknown to us, which have been caused by previous or existing owners or operators of the properties, may exist on the properties in which we hold an interest. In past years we have been engaged in exploration in northern Idaho, which is currently the site of a Federal Superfund cleanup project. Although the Company is no longer involved in this or other areas at present, it is possible that environmental cleanup or other environmental restoration procedures could remain to be completed or mandated by law, causing unpredictable and unexpected liabilities to arise. At the date of this Annual Report, the Company is not aware of any environmental issues or litigation relating to any of its current or former properties.

Future legislation and administrative changes to the mining laws could prevent us from exploring our properties.

New state and U.S. federal laws and regulations, amendments to existing laws and regulations, administrative interpretation of existing laws and regulations, or more stringent enforcement of existing laws and regulations, could have a material adverse impact on our ability to conduct exploration and mining activities. Any change in the regulatory structure making it more expensive to engage in mining activities could cause us to cease operations.

If we establish the existence of a mineral reserve on any of our properties in a commercially exploitable quantity, we will require additional capital in order to develop the property into a producing mine. If we cannot raise this additional capital, we will not be able to exploit the reserve, and our business could fail.

If we do discover mineral reserves in commercially exploitable quantities on any of our properties, we will be required to expend substantial sums of money to establish the extent of the reserve, develop processes to extract it and develop extraction and processing facilities and infrastructure. There can be no assurance that a mineral reserve will be large enough to justify commercial operations, nor can there be any assurance that we will be able to raise the funds required for development on a timely basis. If we cannot raise the necessary capital or complete the necessary facilities and infrastructure, our business may fail.

Land reclamation requirements for our properties may be burdensome and expensive.

Although variable depending on location and the governing authority, land reclamation requirements are generally imposed on mineral exploration companies (as well as companies with mining operations) in order to minimize long term effects of land disturbance.

Reclamation may include requirements to:

- control dispersion of potentially deleterious effluents; and
- reasonably re-establish pre-disturbance land forms and vegetation.

In order to carry out reclamation obligations imposed on us in connection with our potential development activities, we must allocate financial resources that might otherwise be spent on further exploration and development programs. We plan to set up a provision for our reclamation obligations on our properties, as appropriate, but this provision may not be adequate. If we are required to carry out unanticipated reclamation work, our financial position could be adversely affected.

Mineral exploration and development is subject to extraordinary operating risks. We do not currently insure against these risks. In the event of a cave-in or similar occurrence, our liability may exceed our resources, which would have an adverse impact on our Company.

Mineral exploration, development and production involve many risks, which even a combination of experience, knowledge and careful evaluation may not be able to overcome. Our operations will be subject to all the hazards and risks inherent in the exploration, development and production of resources, including liability for pollution, cave-ins or similar hazards against which we cannot insure or against which we may elect not to insure. Any such event could result in work stoppages and damage to property, including damage to the environment. We do not currently maintain any insurance coverage against these operating hazards. The payment of any liabilities that arise from any such occurrence would have a material, adverse impact on our Company.

Estimates of mineralized material are subject to evaluation uncertainties that could result in project failure.

Our exploration and future mining operations, if any, are and would be faced with risks associated with being able to accurately predict the quantity and quality of mineralized material within the earth using statistical sampling techniques. Estimates of any mineralized material on any of our properties would be made using samples obtained from appropriately placed trenches, test pits and underground workings and intelligently designed drilling. There is an inherent variability of assays between check and duplicate samples taken adjacent to each other and between sampling points that cannot be reasonably eliminated. Additionally, there also may be unknown geologic details that have not been identified or correctly appreciated at the current level of accumulated knowledge about our properties. This could result in uncertainties that cannot be reasonably eliminated from the process of estimating mineralized material. If these estimates were to prove to be unreliable, we could implement an exploitation plan that may not lead to commercially viable operations in the future.

Mineral prices are subject to dramatic and unpredictable fluctuations.

Other than from our drilling services subsidiaries, we expect to derive revenues, if any, from the eventual extraction and sale of precious and base metals such as gold, silver and copper. The price of those commodities has fluctuated widely in recent years, and is affected by numerous factors beyond our control including international, economic and political trends, expectations of inflation, currency exchange fluctuations, interest rates, global or regional consumptive patterns, speculative activities and increased production due to new extraction developments and improved extraction and production methods. The effect of these factors on the price of base and precious metals, and, therefore, the economic viability of any of our exploration projects, cannot accurately be predicted.

The mining industry is highly competitive and there is no assurance that we will continue to be successful in acquiring mineral claims. If we cannot continue to acquire properties to explore for mineralized material, we may be required to reduce or cease exploration activity and/or operations.

The mineral exploration, development, and production industry is largely un-integrated. We compete with other exploration companies looking for mineral properties and the minerals that can be produced from them. While we compete with other exploration companies in the effort to locate and license mineral properties, we do not compete with them for the removal or sales of mineral products from our properties if we should eventually discover the presence of them in quantities sufficient to make production economically feasible. Readily available markets exist worldwide for the sale of gold and other mineral products. Therefore, we will likely be able to sell any gold or mineral products that we identify and produce.

There are hundreds of public and private companies that are actively engaged in mineral exploration. Furthermore, since the mineral exploration sphere is so diverse and there are virtually no similar exploration companies with a revenue producing drilling subsidiary, it is quite difficult to identify specific primary competitors and make comparisons to our Company. A representative sample of exploration companies that are similar to our Company in size, financial resources and primary objective include such publicly traded mineral exploration companies as Goldrich Mining Company (GRMC), General Moly, Inc. (GMO), Energold Drilling (EGD), Cabo Drilling (CBE), Klondex Mining (KDX) and Mines Management (MGN).

Many of our competitors have greater financial resources and technical facilities. Accordingly, we will attempt to compete primarily through the knowledge and experience of our management. This competition could adversely affect our ability to acquire suitable prospects for exploration in the future. Accordingly, there can be no assurance that we will acquire any interest in additional mineral properties that might yield reserves or result in commercial mining operations.

Third parties may challenge our rights to our mineral properties or the agreements that permit us to explore our properties may expire if we fail to timely renew them and pay the required fees.

In connection with the acquisition of our mineral properties, we sometimes conduct only limited reviews of title and related matters, and obtain certain representations regarding ownership. These limited reviews do not necessarily preclude third parties from challenging our title and, furthermore, our title may be defective. Consequently, there can be no assurance that we hold good and marketable title to all of our mining concessions and mining claims. If any of our concessions or claims were challenged, we could incur significant costs and lose valuable time in defending such a challenge. These costs or an adverse ruling with regards to any challenge of our titles could have a material adverse effect on our financial position or results of operations. There can be no assurance that any such disputes or challenges will be resolved in our favor.

We are not aware of challenges to the location or area of any of our mining claims. There is, however, no guarantee that title to the claims will not be challenged or impugned in the future.

Acquisitions and integration issues may expose us to risks.

Our business strategy includes making targeted acquisitions. Any acquisition that we make may be of a significant size, may change the scale of our business and operations, and may expose us to new geographic, political, operating, financial and geological risks. Our success in our acquisition activities depends on our ability to identify suitable acquisition candidates, negotiate acceptable terms for any such acquisition and integrate the acquired operations successfully with our own. Any acquisitions would be accompanied by risks. For example, there may be significant decreases in commodity prices after we have committed to complete the transaction and have established the purchase price or exchange ratio; a potential materialized property may prove to be below expectations; we may have difficulty integrating and assimilating the operations and personnel of any acquired companies, realizing anticipated synergies and maximizing the financial and strategic position of the combined enterprise and maintaining uniform standards, policies and controls across the organization; the integration of the acquired business or assets may disrupt our ongoing business and its relationships with employees, customers, suppliers and contractors; and the acquired business or assets may have unknown liabilities which may be significant. If we choose to use equity securities as consideration for such an acquisition, existing shareholders may suffer dilution. Alternatively, we may choose to finance any such acquisition with our existing resources. There can be no assurance that the Company would be successful in overcoming these risks or any other problems encountered in connection with such acquisitions.

Joint ventures and other partnerships in relation to our properties may expose us to risks.

We are currently involved in, and may enter into in the future, joint ventures or other partnership arrangements with other parties in relation to the exploration, development and production of certain of the properties in which we have an interest, particularly the Butte Highlands project. Joint ventures can often require unanimous approval of the parties to the joint venture or their representatives for certain fundamental decisions such as an increase or reduction of registered capital, merger, division, dissolution, amendments of constituting documents, and the pledge of joint venture assets, which means that each joint venture party may have a veto right with respect to such decisions which could lead to a deadlock in the operations of the joint venture or partnership. Further, we may be unable to exert control over strategic decisions made in respect of such properties. Any failure of such other companies to meet their obligations to us or to third parties, or any disputes with respect to the parties' respective rights and obligations, could have a material adverse effect on the joint ventures or their properties and therefore could have a material adverse effect on our results of operations, financial performance, cash flows and the price of the common shares.

Risks Related To Our Company

We have a limited operating history on which to base an evaluation of our business and prospects.

Although we have been in the business of exploring mineral resource properties since our incorporation in 1968, we were inactive for many years prior to our new management in January 2004. Since January 2004, we have not yet located any mineral reserve. As a result, we have not had any revenues from our exploration division, however we do have a drilling services wholly-owned subsidiary which has generated revenues in past fiscal years and which we expect to generate revenues in the future. In addition, our operating history has been restricted to the acquisition and exploration of our mineral properties and this does not provide a meaningful basis for an evaluation of our prospects if we ever determine that we have a mineral reserve and commence the construction and operation of a mine. Other than through conventional and typical exploration methods and procedures, we have no additional way to evaluate the likelihood of whether our mineral properties contain any mineral reserve or, if they do that they will be operated successfully. We anticipate that we will continue to incur operating costs without realizing any revenues (from exploration) during the period when we are exploring our properties.

During the fiscal year ending September 30, 2010, we (the parent company) had losses of \$5,843,114 in connection with the maintenance and exploration of our mineral properties and the operation of our exploration business. We therefore expect to continue to incur significant losses into the foreseeable future. We recognize that if we are unable to generate significant revenues from mining operations and dispositions of our properties, we will not be able to earn profits or continue operations. At this early stage of our operation, we also expect to face the risks, uncertainties, expenses and difficulties frequently encountered by companies at the start up stage of their business development. We cannot be sure that we will be successful in addressing these risks and uncertainties and our failure to do so could have a materially adverse effect on our financial condition. There is no history upon which to base any assumption as to the likelihood that we will prove successful and we can provide investors with no assurance that we will generate any operating revenues or ever achieve profitable operations.

Investors' interests in our Company will be diluted and investors may suffer dilution in their net book value per share if we issue additional employee/director/consultant options or if we sell additional shares to finance our operations.

We have not generated revenue from exploration since the commencement of our exploration stage in January 2004. In order to further expand our company and meet our objectives, capital funding above that provided through anticipated revenues of our revenue producing subsidiary, any additional growth and/or expanded exploration activity may need to be financed through sale of and issuance of additional shares, including, but not limited to, raising finances to explore our newly acquired South Eureka property. Furthermore, to finance any acquisition activity, should that activity be properly approved, and depending on the outcome of our exploration programs, we may also need to issue additional shares to finance future acquisitions, growth and/or additional exploration programs of any or all of our projects or to acquire additional properties. We may also in the future grant to some or all of our directors, officers, insiders, and key employees options to purchase our common shares as non-cash incentives. The issuance of any equity securities could, and the issuance of any additional shares will, cause our existing shareholders to experience dilution of their ownership interests.

If we issue additional shares or decide to enter into joint ventures with other parties in order to raise financing through the sale of equity securities, investors' interests in our Company will be diluted and investors may suffer dilution in their net book value per share depending on the price at which such securities are sold. As of the date of the filing of this report there are also outstanding 8,050,375 common share purchase warrants (exercisable into 8,050,375 shares of common stock), options granted that are exercisable into 6,093,641 common shares, and debt convertible into 3,333,333 common shares. If all of these were exercised or converted, these would represent approximately 24% of our issued and outstanding shares. If all of these warrants and options are exercised and the underlying shares are issued, such issuance will cause a reduction in the proportionate ownership and voting power of all other shareholders. The dilution may result in a decline in the market price of our shares.

Conflicts of Interest

Certain of our officers and directors may be or become associated with other businesses, including natural resource companies that acquire interests in mineral properties. Such associations may give rise to conflicts of interest from time to time. Our directors are required by Delaware Corporation law to act honestly and in good faith with a view to our best interests and to disclose any interest, which they may have in any of our projects or opportunities. In general, if a conflict of interest arises at a meeting of the board of directors, any director in a conflict will disclose his interest and abstain from voting on such matter or, if he does vote, his vote will not be counted.

We have not adopted any separate formal corporate policy regarding conflicts of interest; however other corporate governance measures have been adopted, such as creating a directors' audit committee requiring independent directors. Additionally, our Code of Ethics does address areas of possible conflicts of interest. As of the date of filing of this report, we had six independent directors on our board of directors (Jim Moore, Vance Thornberry, Eric Klepfer, Ron Guill, Robert Martinez, and David Poynton). The Company has formed three committees to ensure our compliance with the requirements of the NYSE Amex. We established an independent audit committee consisting of three independent directors, all of whom were determined to be "financially literate" and one of whom was designated as the "financial expert". We also formed a compensation committee and a corporate governance and nominating committee, both of which are comprised entirely of independent directors. At this time, we feel that these committees and our Code of Ethics provide sufficient corporate governance for our purposes and will meet the specific requirements of the NYSE Amex.

Dependence on Key Management Employees

The nature of both sides of our business, our ability to continue our exploration and development activities and to develop a competitive edge in the marketplace depends, in large part, on our ability to attract and maintain qualified key management personnel. Competition for such personnel is intense, and there can be no assurance that we will be able to attract and retain such personnel. Our development now and in the future will depend on the efforts of key management figures, such as Randal Hardy, Paul Dirksen, Craig Crowell, or Martin Lanphere. The loss of any of these key people could have a material adverse effect on our business. In this regard, we have attempted to reduce the risk associated with the loss of key personnel and have obtained directors and officers insurance coverage. In addition, we have expanded the provisions of our equity incentive plan so that we can provide incentives for our key personnel.

We may not realize the benefits of the Lookout Mountain and other acquired growth projects.

As part of our strategy, we will continue existing efforts and initiate new efforts to develop gold and other mineral projects. We have a larger number of such projects as a result of the acquisition of Staccato Gold, including the Lookout Mountain project. A number of risks and uncertainties are associated with the development of these types of projects, including political, regulatory, design, construction, labor, operating, technical and technological risks and uncertainties relating to capital and other costs and financing risks. The failure to successfully develop any of these initiatives could have a material adverse effect on our financial position and results of operations.

As part of our business model, we pursue a strategy that may cause us to expend significant resources exploring properties that may not become revenue-producing sites, including the Lookout Mountain project.

Part of our business model is to pursue a strategy which includes significant exploration activities, such as proposed exploration at the Lookout Mountain project. Because of the nature of exploration for precious metals, a property's exploration potential is not known until a significant amount of geologic information has been generated. We may spend significant resources exploring the Lookout Mountain project and gathering certain geologic information only to determine that the project is not capable of being a revenue-producing property for us.

If our cash flows prove inadequate to service our debt and provide for our other obligations, we may be required to refinance all or a portion of such existing and future debt at terms that are unfavorable to it.

Our ability to make payments on, and refinance, our debt and other obligations and to fund our operations and capital expenditures will depend on our ability to generate substantial operating cash flow. If our cash flows prove inadequate to meet our debt service obligations, we may be required to refinance all or a portion of our existing or future debt or to sell assets or to obtain additional financing. We cannot assure you that any such refinancing or that any such sale of assets or additional financing would be possible on favorable terms, or at all.

We are required to comply with Canadian securities regulations and be subject to additional regulatory scrutiny in Canada.

We are a ‘reporting issuer’ in the provinces of British Columbia and Alberta since completion of the acquisition of Staccato Gold. As a result, we are subject to increased regulatory scrutiny and costs associated with complying with securities legislation in those provinces. For example, we are subject to civil liability for misrepresentations in written disclosure and oral statements. Legislation has been enacted in these provinces which creates a right of action for damages against a reporting issuer, its directors and certain of its officers in the event that the reporting issuer or a person with actual, implied or apparent authority to act or speak on behalf of the reporting issuer releases a document or makes a public oral statement that contains a misrepresentation or the reporting issuer fails to make timely disclosure of a material change.

We do not anticipate any particular regulation that would be difficult to comply with. However, failure to comply with regulations may result in civil awards, fines, penalties and orders that could have an adverse effect on us.

Certain Risks Associated with Operation of Our Wholly Owned Subsidiary, Timberline Drilling, Inc.

Our subsidiary derives all of its revenues from companies in the mining exploration and production industry, a historically cyclical industry.

Our subsidiary derives all its revenues from companies in the mining exploration and production industry, a historically cyclical industry. Any prolonged reduction in the overall level of exploration and development activities, can adversely impact our subsidiary in many ways by negatively affecting:

- Its revenues, cash flows and profitability;
- Its ability to maintain or increase our borrowing capacity;
- Its ability to obtain additional capital to finance our business and make acquisitions, and the cost of that capital;
- Its ability to retain skilled drilling personnel whom we would need in the event of an upturn in the demand for our services; and
- the fair market value of its rig fleet.

Timberline Drilling may be unable to attract and retain qualified, skilled employees necessary to operate its business.

Timberline Drilling’s success depends in large part on its ability to attract and retain skilled and qualified personnel. The inability of Timberline Drilling officers and management to hire, train and retain a sufficient number of qualified employees could impair the ability to manage and maintain our business. Drilling and drilling related work requires skilled employees who can perform physically demanding work. Shortages of qualified personnel are occurring in this industry. As a result of the volatility of the drilling industry and the demanding nature of the work, potential employees may choose to pursue employment in fields that offer a more desirable work environment at wage rates that are competitive with ours. If Timberline Drilling should suffer any material loss of personnel to competitors or management is unable to employ additional or replacement personnel with the requisite level of training and experience to adequately operate its equipment, its operations could be materially and adversely affected. With a reduced pool of workers, it is possible that it will have to raise wage rates to attract workers from other fields and to retain its current employees. If Timberline Drilling is not able to increase its service rates to its customers to compensate for wage-rate increases, its profitability and other results of operations may be adversely affected.

Shortages in equipment and supplies could limit Timberline Drilling’s drilling operations and jeopardize its relations with customers.

The materials and supplies Timberline Drilling uses in its drilling operations include fuels to operate our drilling equipment, drilling mud, drill pipe, drill collars, drill bits and cement. Shortages in equipment supplies could limit its drilling operations and jeopardize its relations with customers. Timberline Drilling does not rely on a single source of supply for any of these items. From time to time there have been shortages of drilling equipment and supplies during periods of high demand, which we believe could reoccur. Shortages could result in increased prices for drilling equipment or supplies that Timberline Drilling may be unable to pass on to customers. In addition, during periods of shortages, the delivery times for equipment and supplies can be substantially longer. Any significant delays in its obtaining drilling equipment or supplies could limit drilling operations and jeopardize our relations with customers. In addition, shortages of drilling equipment or supplies could delay and adversely affect Timberline Drilling’s ability to obtain new contracts for its drills, which could negatively impact its revenues and profitability.

The mining services industry is a competitive industry.

Contract drilling is a highly competitive industry, where numerous competitors tender bids for contracts. Timberline Drilling’s ongoing ability to continue to secure contracts at a profitable level cannot be assured.

Cyclical downturns in the mining industry could negatively impact Timberline Drilling’s business.

The most significant operating risk is the potential downturn in demand for minerals and metals which would directly impact the need for drilling services. To mitigate this risk the Timberline Drilling is exploiting its competitive advantage in underground drilling.

As the mining cycle lengthens and activity levels increase, the requirement for working capital, particularly accounts receivable and inventory, grows. Accounts receivable levels from junior mining companies typically increase. Junior mining companies are heavily dependent on the capital markets and any change in outlook of the mining sector, or lack of success of their exploration activities, can quickly

TABLE OF CONTENTS

affect their ability to carry on drilling programs. Timberline Drilling manages this risk by closely monitoring accounts receivable aging and the activity of junior mining companies in the capital markets. Deposits and letters of credit are required in some instances.

Levels of inventory increase from increased revenue activity and, potentially, an increase in activity in remote locations. In the event of a sudden downturn Timberline Drilling may be exposed to inventory carrying costs and possible obsolescence. Furthermore it may be difficult and costly to relocate this inventory to other regions. In order to minimize exposure to this risk, Timberline Drilling works closely with its customers to anticipate and plan for scheduled reductions in their drilling programs.

The availability of an adequate workforce cannot be guaranteed and may affect our ability to timely and profitably fulfill our contracts.

From time to time our industry has experienced a shortage of qualified drillers. The industry has gone through downturns that saw many qualified drillers move to other industries. The demand for similar skilled workers in the mining, oil and gas and construction industries also adds to the shortage of qualified people for the drilling services business.

Timberline Drilling has implemented a number of initiatives to retain existing employees and attract new employees, but cannot guarantee that an adequate workforce will be available in the future to meet Timberline Drilling's needs.

Reliance on key accounts.

Timberline Drilling has a small number of accounts that make up the majority of overall revenue and gross profits. When a contract expires or is terminated there is no guarantee that Timberline Drilling has sufficient replacement contracts. Timberline Drilling continues to work with its existing client base and is actively pursuing new clients in order to minimize exposure in this area.

Fluctuations in business costs may affect the profitability of long term contracts.

Timberline Drilling may enter into long term contracts with customers at fixed prices. Timberline Drilling's expenses may vary significantly over a contract period due to fluctuations in the cost of labor, and materials and equipment, consequently creating variations in the profitability of these contracts with fixed prices. Timberline Drilling mitigates this risk by anticipating an escalation in costs when bidding on projects or providing for cost escalation in the contract. However, significant price fluctuations without warning could negatively impact Timberline Drilling's margins.

Extreme weather conditions in certain areas in which Timberline Drilling operates could impact its operations.

Timberline Drilling has operations in the western United States that are subject to extreme weather conditions which can have a significant impact on its operations. In addition, natural and other disasters could have an adverse impact on Timberline Drilling's operations.

Risks Associated With Our Common Stock

Our stock price has been volatile and your investment in our common stock could suffer a decline in value.

Our common stock is traded on the NYSE Amex and the TSX Venture Exchange. The market price of our common stock may fluctuate significantly in response to a number of factors, some of which are beyond our control. These factors include price fluctuations of precious metals, government regulations, disputes regarding mining claims, broad stock market fluctuations and economic conditions in the United States and Canada.

We do not intend to pay any dividends on shares of our common stock in the near future.

We do not currently anticipate declaring and paying dividends to our shareholders in the near future, and any future decision as to the payment of dividends will be at the discretion of our board of directors and will depend upon our earnings, financial position, capital requirements, plans for expansion and such other factors as our board of directors deems relevant. It is our current intention to apply net earnings, if any, in the foreseeable future to finance the growth and development of our business.

ITEM 1B. UNRESOLVED STAFF COMMENTS

Not Applicable.

ITEM 2. DESCRIPTION OF PROPERTIES

Summary of Timberline's Mineral Exploration Prospects

As of December 2010, Timberline has acquired mineral prospects for exploration in Nevada, Montana and Idaho mainly for target commodities of gold, silver, zinc and copper. The prospects are held by both patented and unpatented mining claims owned directly by the Company or through legal agreements conveying exploration and development rights to the Company. Most of our prospects have had a prior exploration history and this is typical in the mineral exploration industry. Most mineral prospects go through several rounds of exploration before an economic ore body is discovered and prior work often eliminates targets or points to new ones. Also, prior operators may have explored under a completely different commodity price structure or technological regime. Mineralization which was uneconomic in the past may be ore grade at current market prices when extracted and processed with modern technology.

Nevada Gold Properties

South Eureka Property (Battle Mountain/Eureka Trend)

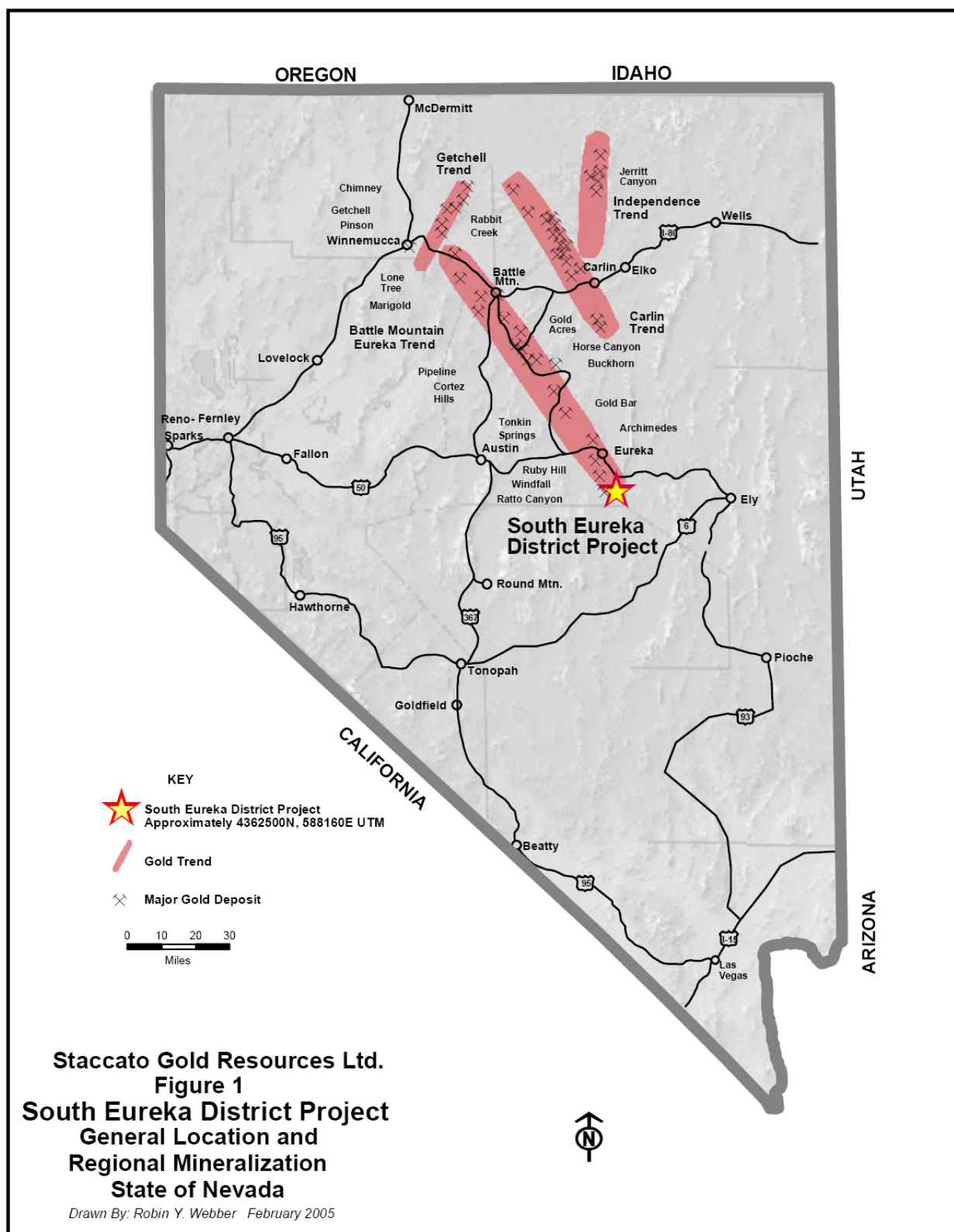
Timberline acquired the South Eureka property as part of its acquisition of Staccato Gold Resources Ltd. ("Staccato Gold") and its wholly owned subsidiary, BH Minerals USA, Inc. ("BH Minerals"), in June 2010. South Eureka comprises an area of approximately 15,000 acres or more than 23 square miles. The property is located approximately 5 miles south of the town of Eureka, Nevada, in the Eureka Mining district within the Battle Mountain – Eureka Trend, also referred to as the Cortez Trend.

The South Eureka property is comprised of 845 unpatented and 15 patented claims and several projects including: Lookout Mountain, Hiero/Syracuse, Windfall Patents, South Ratto, Hoosac/North Amselco, and New York Canyon. Historic open pit mines on the property include: the Windfall pit, the Rustler pit, North and South Paroni pits, and the Lookout Mountain pit. Timberline's database contains over 274,347 feet of drill information from 538 drill holes that have been completed on the property from 1970 through January 2010.

The South Eureka property has no known reserves, as defined under SEC Industry Guide 7 of the United States Securities Act of 1933, as amended, and the proposed program for the property is exploratory in nature.

Property Description

The South Eureka property is located in the southern part of the Eureka mining district of Eureka County, Nevada, within T19N, R53E and unsurveyed T17N and T18N, R53E at the southern end of the Cortez Trend (Battle Mountain/Eureka Trend). The South Eureka property is also within the bounds of the United States Geological Survey "USGS") 1:24,000 scale 7.5 minute topographic series maps of the Pinto Summit and Spring Valley Summit quadrangle.



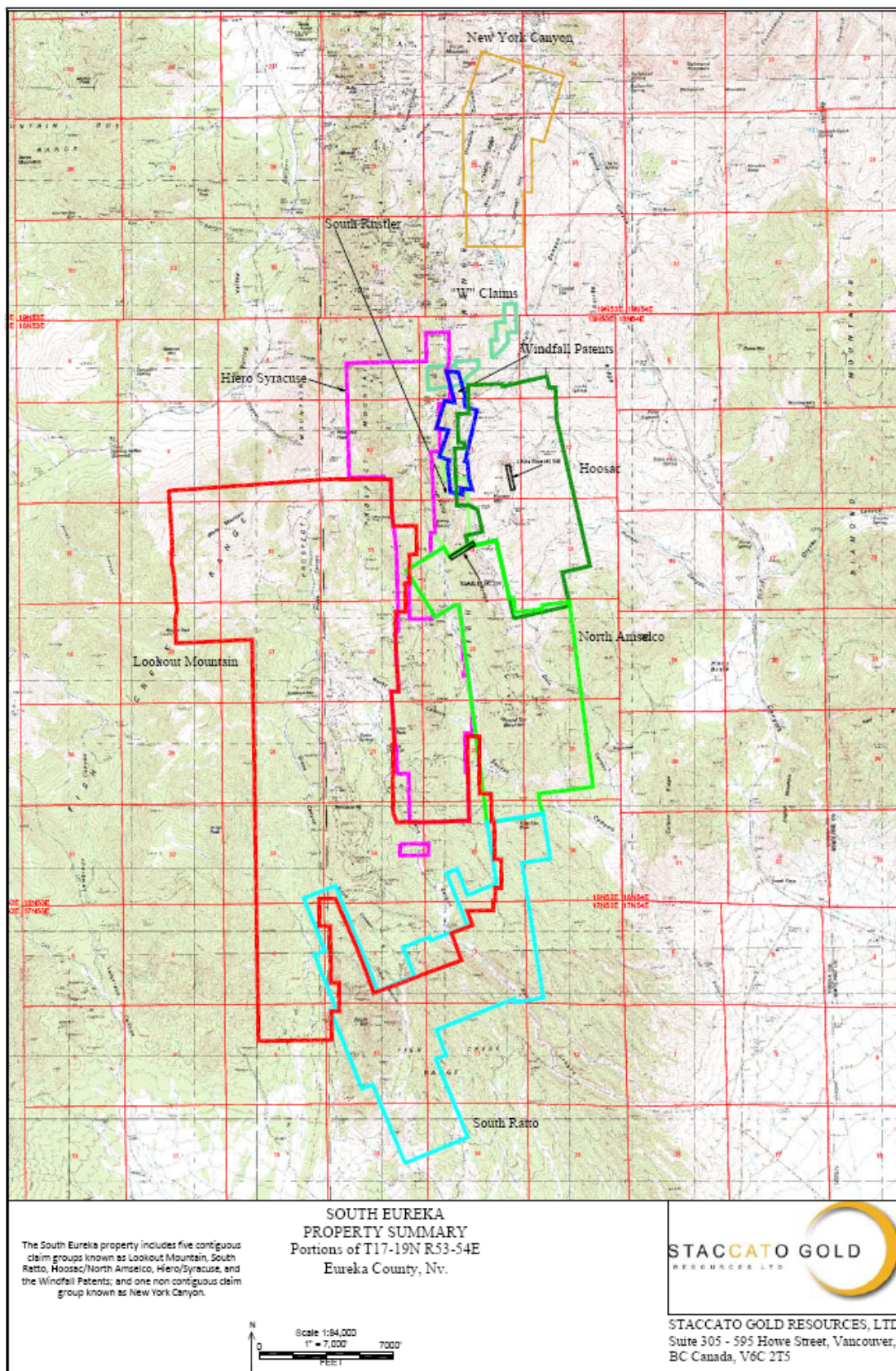


TABLE OF CONTENTS

All unpatented mining claims on the South Eureka property have been located under the General Mining Laws of the United States on US Bureau of Land Management (“BLM”) managed lands.

The Company pays federal and county claim maintenance fees on the South Eureka property. The Federal claim is due to the BLM by September 1st each year, and the remainder is due to Eureka County by November 1st each year. The following table summarizes the claims and royalties for the South Eureka property:

South Eureka Property Claim and Royalty Summary

Property Name & Agreements/Royalties	Type of Claim	Number of Claims	Area
Lookout Mountain Mining lease and agreement dated August 22, 2003, and amended on June 1, 2008, between Timberline and Rocky Canyon Mining Company; 3.5% Net Smelter Return (NSR) royalty + 1.5% NSR royalty capped at \$1.5 million (excludes Trevor and Dave claims); 20 year lease term commencing June 1, 2008; annual advanced royalty payment of \$72,000. (Pending legal opinion, additional 2% NSR possible)	Unpatented	373	2,577 hectares (6,368 acres)
South Ratto Timberline holds title; 4% NSR	Unpatented	108	869 hectares (2,148 acres)
Hoosac/North Amselco Timberline holds title, under lease to DFH, a subsidiary of Royal Gold. Timberline currently pays all claim fees.			
Hoosac 4% NSR + 2% NSR + 0.75% NSR	Unpatented	98	580 hectares (1,434 acres)
Little Rosa (Hoosac royalty applies)	Patented	1	
North Amselco 4% NSR + 1% NSR + 1.6% NSR + 0.75% NSR	Unpatented	94	690 hectares (1,707 acres)
Rambler (North Amselco royalty applies)	Patented	1	
South Rustler/W-Claims Claims owned by DFH Co., a subsidiary of Royal Gold, Inc. Draft agreement in place pursuant to which Timberline would acquire the 16 claims, subject to the following royalties: 4% NSR + 2% NSR + 0.75% NSR. The Hoosac/North Amselco lease agreement would then cancel.	Unpatented	16	112 hectares (278 acres)
Hiero/Syracuse Timberline holds title. (Includes 2 mill sites on Syracuse 1 & 2) (Pending legal opinion, 2% NSR possible)	Unpatented	111	765 hectares (1,892 acres)
Windfall Patents Mining lease and option agreement between Timberline and Century Gold. Annual lease payment of \$48,000; April 1, 2012 lease term; property may be purchased anytime before February 28, 2012 for \$750,000; 4% NSR	Patented	13	67 hectares (166 acres)
New York Canyon Timberline holds title; 4% NSR + 1.5% NSR	Unpatented	45	343 hectares (847 acres)
Total Unpatented Lode Claims		845	6,003 hectares (14,833 acres)
Total Patented Lode Claims		15	

Timberline has the right to explore and develop the Lookout Mountain project subject to a mining lease and agreement dated August 22, 2003 with Rocky Canyon Mining Company, and amended on June 1, 2008. The lease term was extended to 20 years on June 1, 2008, and thereafter for as long as minerals are mined on the project. Advanced royalty payments are \$6,000 per month, or \$72,000 per annum. The work commitment on the project has been fulfilled. A 3.5% net smelter return royalty, plus a 1.5% net smelter return royalty capped at \$1.5 million (excludes Trevor and Dave claims) exists on the project. In addition, a 2% NSR royalty may exist, pending a legal opinion that is forthcoming.

TABLE OF CONTENTS

Monthly lease payments of \$4,000, or \$48,000 per annum, are due to maintain the Windfall Patents in good standing. Staccato has the option to purchase the project for US\$750,000 if the option is exercised before February 2012. The term of the agreement extends until April 2012. A 4% net smelter return royalty exists on the project.

The Hiero/Syracuse, South Ratto, and New York Canyon projects are owned by the Company subject to royalty agreements. Net smelter return royalties up to 5.5% exist on the projects. Pending a legal opinion that is forthcoming, the same 2% NSR royalty referenced above may exist on the Hiero/Syracuse project.

The Hoosac/North Amselco project is comprised of the Hoosac, North Amselco, and South Rustler/W-claim groups. The Hoosac and North Amselco claims are owned by the Company and are currently under lease to DFH Co., a subsidiary of Royal Gold, Inc. No payments are due under the lease agreement. The South Rustler/W-Claims are owned by DFH Co. A draft agreement is in place pursuant to which the Company would acquire the South Rustler/W-Claims, and the Hoosac/North Amselco lease agreement would cancel. Net smelter return royalties ranging from 6.75% to 7.35% exist on the projects. Timberline currently pays all of the claim maintenance fees for the Hoosac/North Amselco project.

Accessibility, Physiography, Climate and Infrastructure

The South Eureka property is located 5 miles south and southwest of the town of Eureka, within the southern part of the Eureka Mining district of Eureka County, Nevada. The South Eureka property is located at the southeastern end of the Battle Mountain/Eureka Trend (Cortez Trend) of gold and base-metal deposits in north-central Nevada.

The South Eureka property is situated in north-central Nevada in an area with established mining infrastructure. Transmission power lines serve Eureka from the north. All essential services such as food and lodging are available in Eureka, including the dockage for shipments of heavy equipment. A small airport at Eureka is available for private air transport. Railroad access also is available in the area. The gold mines of north-central Nevada continue to produce a significant portion of the world's gold, and skilled miners and mining professionals are available in Eureka, and 100 miles to the north in Carlin, Elko, and Spring Creek. Permitting a mining operation in Nevada has been a process with which local, state and federal regulators are very familiar and generally cooperative.

Terrain on the South Eureka property is rugged, with high ridges, steep canyons, and narrow valleys. Elevations range from 7,000 to 9,000 feet. Ridges show abundant bedrock exposures, slopes and valleys are typically covered by soil and alluvium. Sagebrush abounds in lower-elevation areas while juniper and pinion cover the higher elevations. Grasses and shrubs grow on the highest ridge tops. The climate of the project area is semi-arid with the area receiving moderate winter snows and occasional summer thunderstorms, with heavy rain from time to time during otherwise hot and dry summers. In winter, access is not maintained off the paved roads and November snow commonly lingers until April.

U.S. Highway 50 passes to the east of the South Eureka property and access is gained by heading south out of Eureka on the Highway and connecting with unpaved local roads, some of which are periodically maintained by Eureka County. The turnoff for the New York Canyon claim group is about a half mile south of Eureka on U.S. Highway 50 and is an unpaved road running up New York Canyon to the east side of the claim group.

The Windfall group and the northern parts of the Hoosac and Lookout Mountain groups are accessed by the Windfall Canyon Road and its westward extension (the former haul road for the Lookout Mountain Mine), which turns southwest off U.S. Highway 50 approximately 2 miles south of Eureka.

The southern parts of the South Eureka property are accessed by traveling approximately 8 miles south of Eureka on U.S. 50 to South Gate, then 1 mile south-southwest on the Fish Creek Valley road to the unimproved Secret Canyon Road, then northwest to the southern part of the Hoosac bloc. Approximately 2 miles from South Gate on the Fish Creek Valley Road, a turnoff to the west and northwest on the Ratto Canyon Road accesses the southern portion of the Lookout Mountain group. Many dirt tracks within the South Eureka property allow additional access.

Summer temperatures usually consist of many consecutive days of over 90° F (32.2° C), and temperatures can reach as high as 100° F (40.6° C) or more. Winter temperatures generally range from as cold as below 0° F (17.8° C) to usually in the 20° to 35° F (-6.67° to 1.7° C) range. Precipitation amounts vary from year to year, averaging about 10.0 inches (25.4 cm) for the area. Several feet of snow usually accumulate on the property during the winter months.

Historic Exploration

The most significant exploration on the South Eureka property has been the drilling programs mounted over recent years. Such exploration on the South Eureka property spans a period of over twenty years. Drilling on the Hoosac and Windfall blocs date from Norse-Windfall (63 holes, 1970s-1980s), Amselco (8 holes, mid-1980s), Tenneco (18 holes, 1989-1991), Pathfinder (18 holes, 1993) and Pathfinder/Cambior (36 holes, 1995-1997). On the Lookout Mountain claim group, drilling programs began with Amselco (296 holes, 1978-1985) followed by the Windfall group (20 holes, 1986), EFL Gold Company (10 holes, 1990), Barrick (40 holes, 1992-93), and Echo Bay (70 holes, 1994-95). The drilling programs were conducted concurrent with and guided by extensive geologic mapping, geochemical rock and soil sampling programs and air and ground geophysics. Geological mapping and geochemical programs were very successful in discovering target areas characterized by permissive structures and traces of gold with arsenic, antimony, and mercury toxic element anomalies in soil and rock.

TABLE OF CONTENTS

The methods of collection and analyses of some historical soil and rock samples were not always available in the data, but it is likely that the samples were collected, documented, prepared and analyzed to the standards of professional diligence and analytical techniques applicable at the time. The importance of a geochemical-geological exploration approach is evidenced by the fact that the drilling of many such anomalies has resulted in significant indications of disseminated gold mineralization. The Windfall, Rustler, and Paroni deposits on the Windfall claims and the Lookout Mountain on the Lookout Mountain group were discovered by drilling soil and rock anomalies in permissive structural and stratigraphic settings. Drill testing of several geochemical anomalies in permissive geological settings has also resulted in the discovery of several promising zones of gold mineralization on the Hoosac, Windfall, and Lookout Mountain claim groups. As yet, these zones have not been fully tested.

Amselco Exploration began exploring the Lookout Mountain project in 1978, conducting an extensive geologic mapping, soil and rock sampling and an initial 15-hole reverse circulation drilling program which tested gold mineralization along the Ratto Ridge Fault and associated geochemical anomalies and jasperoids developed along the N-S trending Ratto Ridge. This drilling discovered significant sediment-hosted disseminated gold mineralization at depth. Amselco drilled 296 holes between 1978 and 1985. Amselco also discovered five other areas along Ratto Ridge which contain partially developed gold resources. These areas are located at South Lookout Mountain, Pinnacle Peak, Triple Junction, South Ratto Ridge, and South Adit. In 1986, while Amselco was in process of becoming BP Minerals, Amselco management decided that the Lookout Mountain deposit was not of further interest even though their geologists reportedly believed the deposit had significant potential. The property was optioned to a joint venture of three companies which then owned Norse-Windfall Mines, the Eureka Venture.

Windfall continued work at Lookout Mountain, drilled 11 exploration holes, and decided that the deposit had a total of 446,246 in place tons with an average grade of 0.12 oz of gold/ton.

In 1990, EFL Gold Mines took bulk samples from the floor of the Lookout Mountain pit. These samples returned assays values ranging from 0.10 to 0.135 oz of gold/ton. EFL also drilled 9 holes, two of which, drilled 500 feet (152 meters) into the floor of the pit, showed both oxide and sulfide gold mineralization.

Barrick (1992-93) completed geologic mapping, took more than 500 soil samples to expand and fill in Amselco's grid, and drilled in various places, primarily along Ratto Ridge and for a mile or so north of the ridge. Drilling targeted favorable stratigraphy at depth near fault intersections. Barrick discovered that geochemical anomalies are apparently controlled by E-NE and N-NW to NW trending cross structures which intersect the N-S trending Ratto Ridge Fault. Much of the Barrick work focused on the deeper potential in Cambrian Dunderberg Shale east of the Ratto Ridge Fault, and potential in the Devonian Nevada Group, especially the Bartine Limestone west of the fault. Outcrops of Bartine Limestone in the area show weak gold mineralization, strong alteration, and anomalous pathfinder element geochemistry. Barrick drilled 38 holes to a maximum depth of approximately 1,500 feet and encountered several sulfide gold intercepts.

Work by Barrick also included air and ground geophysics, and a stratigraphic and mineralogic geochemical study in conjunction with geologic mapping, developed and prioritized several target areas. Approximately 800 rock samples were collected and had high-quality multi-element analyses run, ICP and graphite furnace analyses at MB Associates in California, and ICP and neutron activation analysis at Activation Laboratories in Canada. Mapping, together with results of the Magmachem geochemistry, indicated that mineralization was apparently strongly controlled by E-NE and N-NW to NW trending cross structures near or at the point they intersect the N-S trending Ratto Ridge Fault and the Cambrian Dunderberg Shale and Hamburg Dolomite. Ultimately, Barrick drilled 40 reverse circulation holes. However, geological and geochemical targets or additional drilling in areas of known mineralization previously discovered by Amselco found insufficient mineralization to meet Barrick's objectives. It should be noted that the potential for mineralization west of the Ratto Ridge crest has not been explored adequately.

Echo Bay (1993-95) not only worked Ratto Ridge but also acquired additional ground to the north, south, and southwest. They conducted mapping, sampling, and scattered drilling in the area, exploring deep high-grade potential in the Cambrian Dunderberg Shale and Hamburg Dolomite, and testing Devonian Nevada Group targets west of the Ratto Ridge Fault. Echo Bay drilled several promising holes, including drill hole EBR 27 which intersected 110 feet grading 0.043 oz of gold/ton in the Dunderberg, and drill hole EBR-9 which intersected 115 feet grading 0.043 oz of gold/ton in the Nevada Group. Offsets of EBR-9 found 90 feet grading 0.028 oz of gold/ton, and another hole which was lost before reaching planned depth found 45 feet of 0.024 oz of gold/ton. Further offsets of EBR-9 and several widely-spaced holes averaging 2,000 feet deep (EBR 15, 16, 17, 18, and 20) found some anomalous gold along Ratto Ridge but no major intercepts. Eventually, the Echo Bay project totaled 104 RC holes. Faced with depletion of budgets with no significant exploration success, the decline in gold prices and large land payments, Echo Bay decided to drop the property.

On the Windfall, Hoosac, and New York Canyon claim groups, Bill Wilson of the Idaho Mining Corp, then Windfall Venture, later Norse-Windfall, initiated reconnaissance mapping, soil and rock chip sampling, trenching, and drilling in the early 1970s. He noted that the original underground Windfall Mine, which was discovered in 1908 and produced approximately 65,000 tons of 'invisible gold' mineralized rock grading 0.368 oz/ton, was a Carlin-type sediment-hosted disseminated gold occurrence. Wilson's work emphasized the east side of Hamburg Ridge, the Windfall Trend, where he drilled, with conventional air rotary, holes F1 through F20, and Z-1 through Z-31, Z42, and ZA-1 on the current Windfall group. He drilled holes Z32-41 on the Hoosac group. The drill holes were generally from 50 to 250 feet deep. Six of Wilson's original forty-three Z-holes intersected gold mineralization exceeding 0.02 oz of gold/ton. This success led to infill drilling and the development of the Windfall open pit mine in 1975, and soon thereafter, the Rustler and Paroni open pit mines. Gold was extracted in a CN heap-leach operation from sanded and silicified dolomite and silicified shale.

TABLE OF CONTENTS

No geologic maps exist from this period other than a few maps compiled from USGS work. Although many drill hole location maps are archived in Century Gold files, the coordinates for many drill hole collars are not available, very few collars are visible in the field, and assay data from infill drilling is poorly documented.

Recent Activity

The Company continues to work toward completion of a comprehensive technical work program at its South Eureka property. A large part of the Lookout Mountain project and Windfall Patents project areas have now been mapped and sampled, including a detailed program conducted over the main resource area. The principle objectives of the mapping and sampling program were to characterize offsets along the main mineralized fault zones at Windfall and Lookout Mountain, identify orientations of mineralized cross structures intersecting the main structural zones, and follow up on soil anomalies. The mapping program, combined with surface sampling and acquisition of historic data, has provided a clearer understanding of the structures along Ratto Ridge, as well as identified several significant new exploration target areas.

Over 400 drill holes have been re-logged to ensure geologic consistency with surface mapping, and based on this work, new geologic cross sections and plans have been constructed for the entire Lookout Mountain deposit. Geologic grade shells have also been built, and construction of a 3-D model of the geology, based on the results of historic drill re-logging and mapping efforts, is ongoing. This new work and the updated resource estimate will resolve technical issues identified in the past, and provide Timberline with a plan for advancing the property into the scoping/pre-feasibility study phase following one more round of drilling.

An exploration Plan of Operations has been approved by the BLM and the State Department of Environmental Protection (NDEP) for the Lookout Mountain project. The Plan of Operations calls for approximately 246 acres of disturbance that can be accessed for use in a phased approach, and covers the entire Ratto Ridge structural zone. The Plan of Operations will allow us to complete additional infill, metallurgical, and exploration drilling necessary to advance the development of the Lookout Mountain project.

Scoping Study

Staccato Gold retained SRK Consulting U.S. Inc. (SRK) to complete a preliminary economic scoping study of the Lookout Mountain project in 2007. The study was not completed when it became evident that more technical data was needed to assess the economics of the project, and that SRK had issues with some of the methodology used in the earlier mineralization estimate. Specifically, SRK identified that grade shells were not used appropriately to limit tons and grade estimation. In addition, SRK is of the opinion that insufficient geological constraints were employed in the resource estimation which could lead to inflated numbers. SRK also believes the density values used in the tonnage calculations were too high, and that in its opinion, additional density determinations are required to improve tonnage calculations in the Lookout Mountain mineralized material estimate.

Technical Work Program

In order to improve understanding of the technical aspects of the project, address the issues noted by SRK, and evaluate the potential of the South Eureka property, Staccato Gold initiated a comprehensive work program in June 2008. The program included geologic modeling that incorporated structural and stratigraphic controls to mineralization, additional density determinations, and new drilling and metallurgical test data. The results of this work will be incorporated into the updated mineralization estimate for the Lookout Mountain project.

The 2005-2007 core drilling program completed by Staccato Gold provided data to better define the higher-grade breccia-hosted gold zones at the Lookout Mountain pit, and discovered new areas of mineralization. The core drilling demonstrated the stratabound nature of the gold mineralization in thick zones of collapse breccia within carbonate rock flanking the Ratto Ridge structural zone. Metallurgical and other technical characteristics of known mineralization at Lookout Mountain have not been thoroughly investigated.

Windfall

Staccato Gold completed a ten hole drill program totaling 8,030 feet at its South Eureka property in October 2009. The drilling program focused on testing the extent of gold mineralization at the Windfall project, which is located approximately 3 miles northeast of the main Lookout Mountain project resource area. The Windfall project is one of several prospective gold projects on the Company's extensive South Eureka property in Nevada.

Results from the surface mapping program, historic production and geologic maps, and drilling indicate that high grade gold is locally controlled within cross structures cutting the main Windfall fault zone, at the contact between the Hamburg Dolomite and Dunderburg Shale. The recent drill program tested approximately 3,600 feet of the Windfall fault zone with wide spaced drilling. The Windfall fault zone is part of an extensive mineralized structural trend which extends for over 17,000 feet based on historic data.

All holes in the recent exploration program encountered thick intercepts of low grade gold (holes 5–12) or anomalous gold mineralization (holes 13 and 14) within the Windfall fault zone. The offset and exploration holes drilled define the Windfall fault zone as a (150 to 200 foot) thick zone striking roughly north-south and dipping approximately 60 degrees to the east, containing two or more significant zones of mineralization.

Five of the ten holes were drilled as offsets to follow up on the high grade gold intercept drilled in hole 4 (75 feet at 0.153 ounces of gold/ton), and five were drilled as exploratory holes to test the strike and dip extent of the Windfall fault zone. Several thick intercepts of

TABLE OF CONTENTS

gold mineralization were returned, including 135 feet at 0.011 ounces of gold/ton in hole 7, 135 feet at 0.016 ounces of gold/ton in hole 8, 115 feet at 0.010 ounces of gold/ton in hole 9, and 100 feet at 0.018 ounces of gold/ton in hole 11.

A secondary hanging wall structure identified by the mapping program was also encountered in drill holes 7, 8, 11, and 13 and is characterized by strong silicification and decalcification of Windfall Formation and Dunderberg shale in the hanging wall side of the fault, and Dunderberg shale and Hamburg Dolomite on the footwall side. Drilling indicates a down to the east offset of the Dunderberg – Hamburg contact. This secondary structure represents an attractive and untested target at depth.

Timberline intends to continue to assess the potential of the prospective Windfall fault zone at depth and on strike along the regional trend, with additional surface mapping, sampling, geophysical surveys, and exploration drilling programs planned for the future.

South Eureka Property Exploration Potential

We are of the opinion that the South Eureka property has excellent potential for continued exploration success both at the deposit scale and on the regional scale. The current Lookout Mountain mineralization is defined over a relatively small area at the north end of a mineralized structural corridor that extends for several thousand feet across the property, and up to 4 to 5 kilometers (2.5 to 3 miles) in strike length. This structure hosts several areas of drill indicated mineralization and the exploration potential in this corridor is strong, as evidenced by historic drilling, and soil and rock geochemical analyses. The Lookout Mountain mineralization itself is open for expansion at depth and along strike, especially to the south. Regionally, several other target areas also exist where historic production and exploration have occurred, but only limited systematic exploration has been conducted.

South Eureka Property Ownership

Staccato amended the Lookout Mountain project lease agreement in June 2008. The lease term was extended to 20 years, and thereafter for as long as minerals are mined on the project. Advanced royalty payments are \$72,000 per annum. Pursuant to the amended lease, annual minimum exploration expenditures of \$250,000 are required for five years commencing on June 1, 2008, and an additional expenditure of \$250,000 is required before June 1, 2016, for a total minimum work commitment of \$1,500,000. Exploration expenditures in excess of \$250,000 in any year can be accumulated and carried forward and credited to expenditures required in succeeding years. The Company has fulfilled the work commitment on the Lookout Mountain project.

Monthly lease payments of \$4,000 are due to maintain the Windfall Patents in good standing. Timberline has the option to purchase the project for \$750,000 if the option is exercised before February 2012. The term of the agreement extends until April 2012.

The other projects that comprise the extensive South Eureka property, including the Hiero/Syracuse, South Ratto, New York Canyon, and a large portion of the Hoosac/North Amselco projects, are owned by Timberline subject to underlying royalty agreements. The Company is in the process of consolidating the ownership of a portion of the Hoosac/North Amselco project that is currently held by another party.

South Eureka 2010 Program

Upon receipt of final approval from the BLM, Timberline commenced an aggressive \$2,500,000 work program on the South Eureka property. The program objective was designed to obtain sufficient data to complete a NI 43-101 compliant resource estimate, conduct metallurgical studies and tests, and detail map the geology of the property to better understand the controls of mineralization and to outline additional exploration drill targets for testing in 2011. The information generated by this program is expected to be incorporated into a preliminary economic assessment during the year ended September 30, 2011.

The program to achieve these corporate objectives includes:

- 7,500 foot core drill program focused primarily on obtaining core for process metallurgical scoping studies;
- 30,000 foot Reverse Circulation (RC) drill program directed primarily at in-fill and resource definition drilling necessary to complete a NI 43-101 technical report, including a compliant resource, for the Lookout Mountain Project by early March 2011;
- Drill testing of high grade sulfide/refractory lenses within the oxide resource to better understand the controls and geometry of the sulfide mineralization;
- Metallurgical testing on core samples to define the heap leach characteristics and process parameters;
- Channel sampling and bulk sampling within the historic Lookout Mountain pit for bench-scale metallurgical testing;
- Detailed geologic mapping and sampling to identify and target additional exploration targets on the South Eureka Property but outside of the main Lookout Mountain mineralization area, to be tested during 2011 field season;

As of September 30, 2010 Timberline is on schedule and has one Timberline Drilling core rig and two RC rigs operating on site. The metallurgical scoping study has been formalized, and geologic mapping is on-going. All drilling and geologic mapping will be completed by December 31, 2010, and metallurgical testing commenced in November 2010.

ICBM Project (Cortez/Battle Mountain Trend)

The ICBM Joint Venture Project (Timberline/Barrick) is located in the Battle Mountain Mining District, Lander County, Nevada. The land position consists of 526 hectares (1,300 acres) on BLM administered lands. The drilling to date has demonstrated that mineralization is

TABLE OF CONTENTS

present and is localized along the contacts of Cambrian sediments and altered granodiorite. This style of mineralization is being mined at Newmont's Fortitude/Phoenix complex to the south. Timberline is the operator of the joint venture, and currently holds a 72% interest in the project, with Barrick Gold holding the remaining interest.

As of September 30, 2010, Timberline does not consider the ICBM prospect to be a material property. No material future expenditures are planned on the prospect at this time.

Evan's Mine Project (Carlin Trend)

Staccato acquired an option on the Evan's Mine claims in 2007. The Evan's claims are located adjacent to Newmont's Emigrant Springs development project on the Carlin Trend.

Staccato commenced a three-hole 1,370 meter (4,500 foot) core exploration drilling program on the Evan's Mine property in December 2007, and completed the program in March 2008. No significant gold values were returned, however, anomalous arsenic and mercury were associated with anomalous gold in hole ES-1, and scattered zones of anomalous concentrations of antimony with mercury were present in all holes.

The annual advanced royalty payments on the property were cancelled by agreement with the leaseholder in December 2008. The Company is required to spend a minimum of US\$50,000 on exploration annually, or pay US\$10,000 cash in lieu of the work commitment, to maintain its ownership interest of the property. Excess exploration expenditures in any year can be carried forward. The term of the lease is for an initial 10 year period, and thereafter for as long as the work commitments are made. An NSR from 1% to 2%, based on the gold price, is due to the original property owner. Staccato's exploration program expenditures prior to its acquisition by Timberline satisfied the work commitment for several years.

As of September 30, 2010, Timberline does not consider the Evan's Mine prospect to be a material property. No material future expenditures are planned on the prospect at this time.

Montana Gold Properties

Butte Highlands Gold Project

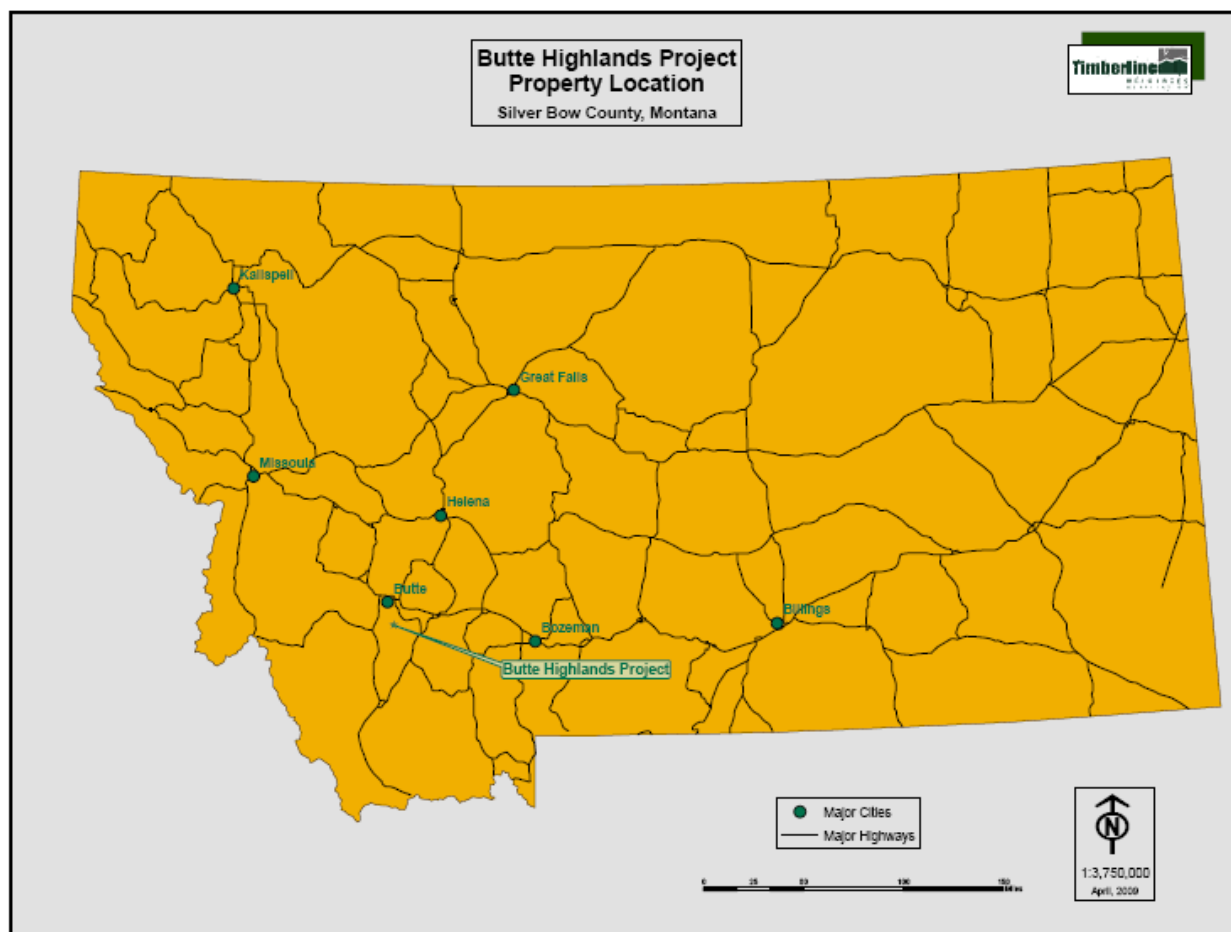


TABLE OF CONTENTS

In July 2007, Timberline closed its purchase of the Butte Highlands Gold Project, including 100-percent ownership of mineral rights, from Butte Highlands Mining Company for \$405,000 cash and 108,000 shares of Timberline common stock. The project is located approximately 15 miles south of Butte, Montana in Silverbow County. The property covers 1,142 acres consisting of a combination of patented and unpatented mining claims situated within Sections 31 and 32, Township 1 North, Range 7 West; Sections 5 and 6, Township 1 South, Range 7 West; and Section 1, Township 1 South, Range 8 West, Montana Principal Meridian. The property can be accessed utilizing motor vehicle via State Highway 2 and County and US Forest Service maintained, improved surface roads. The project is within a favorable geologic domain that has hosted several multi-million ounce gold deposits.

In October 2008, the Company announced that it had agreed to form a 50/50 joint venture with Small Mine Development (“SMD”) at the Butte Highlands project. In July 2009, the Company finalized the joint venture agreement with Highland Mining, LLC (“Highland”) (an affiliate of SMD) to create Butte Highlands JV, LLC (“BHJV”). Under terms of the joint venture agreement, Timberline will be carried to production by Highland, which will fund all mine development costs and began development in the summer of 2009. Both Timberline’s and Highland’s 50-percent share of costs will be paid out of proceeds from future mine production. Under the terms of the operating agreement, filed with this Annual Report as Exhibit 10.21, Highland will have preferential rights with respect to distributions until the investment by the Company is deemed equal to the investment by Highland.

BHJV has continued the exploration plan and geologic modeling of the Butte Highlands project with Timberline’s assistance. During the year ended September 30, 2009, a permit to perform additional exploration, consisting of installing an underground exploration ramp to access mineralization for underground drilling, bulk sampling and metallurgical testing was approved by the State of Montana. Upon approval, construction of the underground ramp and associated development on the project began in August 2009. Completion of the underground ramp, underground drilling and bulk sampling will take approximately 12 to 18 months in total. During the year ended September 30, 2010 BHJV submitted an application for an Operating Permit with the state of Montana to commence gold mining operations. BHJV will be conducted or contracted all base line studies to facilitate the permit. The state of Montana has indicated to Timberline that this process and regulatory approval will take approximately 12 to 18 months. Therefore, Timberline expects to transition directly from exploration to gold mining operations.

Highland, our 50/50 joint venture partner on the project, will carry all costs incurred on the project until mining operations commence. The Company expects that the total costs incurred by Highland on the project to reach this milestone will be between \$20 million and \$24 million.

Butte Highlands Claim Summary

Claim Name(s)	Claim Type	Land Type	Rights	Ownership
BHC 1 thru BHC 61	Unpatented lode	Federal	mineral	100 % Timberline Resources Corp.
MC 1 thru MC 48	Unpatented lode	Federal	mineral	50 % Timberline Resources Corp. ⁽¹⁾
J.B. Thompson	Patented lode	Private	mineral and surface	50 % Timberline Resources Corp. ⁽¹⁾
Main Ripple	Patented lode	Private	mineral and surface	50 % Timberline Resources Corp. ⁽¹⁾
Murphy	Patented lode	Private	mineral and surface	50 % Timberline Resources Corp. ⁽¹⁾
Only Chance	Patented lode	Private	mineral and surface	50 % Timberline Resources Corp. ⁽¹⁾
Purchase	Patented lode	Private	mineral and surface	50 % Timberline Resources Corp. ⁽¹⁾
Red Mountain	Patented lode	Private	mineral and surface	50 % Timberline Resources Corp. ⁽¹⁾
Main Chance	Patented lode	Private	mineral and surface	100 % Richardson Family Trust ⁽²⁾
Island	Patented lode	Private	mineral and surface	100 % Richardson Family Trust ⁽²⁾
Atlantic	Patented lode	Private	mineral and surface	100 % Richardson Family Trust ⁽²⁾
Barnard	Patented lode	Private	mineral and surface	100 % Richardson Family Trust ⁽²⁾
Pony Placer	Patented Lode	Private	surface	50 % Timberline Resources Corp. ⁽¹⁾

⁽¹⁾ Claims are owned 100% by Butte Highlands JV, LLC, of which Timberline Resources owns a 50% interest.

⁽²⁾ Timberline holds a lease option agreement on these claims subject to a mining lease/option to purchase agreement dated October 1, 2009.

All of the unpatented claims are exploration lode claims legally located under federal and state guidelines whereas each claim is 600 feet by 1500 feet encompassing 20 acres. Each claim is clearly marked with a 4 inch by 4 inch post or equivalent tree at each corner and a location monument is erected along the center line of the long direction of the claim. All BLM maintenance requirements have been met.

All of the private lands within the Butte Highlands property are historic lode and placer claims which were patented through the U.S. Government patent process. Timberline Resources is responsible for paying yearly BLM maintenance fees on all unpatented mining claims and Montana State property taxes on all patented lands. All associated taxes and fees are paid up to date as of September 30, 2010. Electricity and water are readily available on the property. If necessary, additional electricity requirements may be met by augmenting the currently available electrical supply with generator power.

[TABLE OF CONTENTS](#)

On October 1, 2009, the Company signed a Mining Lease/Option to Purchase Agreement with the Richardson Family Trust for certain patented claims as detailed in the table above. The Agreement calls for an initial payment of \$20,000 with annual payments of \$15,000, increasing to \$20,000 plus an annual inflation adjustment by October 2013, and remaining at that level thereafter. The Company will pay a 3-4% NSR royalty on any production from the Richardson Family Trust property, based upon the sale price of minerals produced from the property.

Gold mineralization at Butte Highlands is hosted primarily in lower Paleozoic Wolsey shale with higher-grade mineralization occurring within the sediments proximal to diorite sills and dikes. Between 1988 and 1996, prior operators Placer Dome, Battle Mountain, ASARCO, and Orvana Minerals demonstrated the presence of a wide and continuous mineralized zone by drilling 46 core holes (36,835 feet) and 132 reverse-circulation holes (61,338 feet) within the district. The vast majority of this drilling was conducted in the Nevin Hill area which is included in the Timberline property. Best gold intercepts achieved at Butte Highlands include 49.8 feet of 0.651 ounces per ton (oz/t) and 11.5 feet of 1.996 oz/t from surface and 31.0 feet of 1.060 oz/t from underground.

Historic Drilling Highlights (from Surface)

Drill Hole	From (ft)	To (ft)	Length (ft)	Gold (oz/t)⁽¹⁾
DDH 88-3	745.0	756.0	11.0	0.110
	1,070.0	1,085.0	15.0	0.206
DDH 89-1	1,177.2	1,227.0	49.8	0.651
PD 89-1	1,351.0	1,366.0	15.0	0.340
PD 89-2	1,396.0	1,412.0	16.0	0.135
BH 93-1	885.0	895.0	10.0	0.138
	925.0	935.0	10.0	0.319
BH 93-8	1,189.0	1,200.0	11.0	0.131
BH 93-11	758.5	770.0	11.5	0.351
	825.0	845.0	20.0	0.114
	964.0	978.0	14.0	0.776
BH 93-12	762.5	786.0	23.5	0.548
BH 94-2	1,240.0	1,270.0	30.0	0.214
BH 94-3	1,129.3	1,141.0	11.7	0.255
	1,163.4	1,181.0	17.6	0.142
	1,312.0	1,325.5	13.5	0.492
	1,425.0	1,437.0	12.0	0.276
BH 94-16	1,335.5	1,347.0	11.5	0.165
BH 94-17	1,295.5	1,323.0	27.5	0.268
BH 95-5	1,429.0	1,457.5	28.5	0.338
	1,512.5	1,522.5	10.0	0.129
BH 96-1	697.0	722.3	25.3	0.153
	754.0	779.5	25.5	0.158
BH 96-5	837.0	849.0	12.0	0.678
	902.0	916.0	14.0	0.114
	932.5	944.0	11.5	1.996
BH 96-6	1,258.0	1,270.0	12.0	0.142
	1,320.0	1,333.0	13.0	0.165
BH 96-8	1,222.0	1,233.0	11.0	0.234
	1,287.0	1,307.0	20.0	0.212
BH 96-9	993.0	1,012.0	19.0	0.133

(1) All values represent either a single interval or were composited using a weighted average based on sample interval length.

The following table includes highlights from past underground drilling programs conducted in the early-1940s.

Historic Drilling Highlights (from Underground)

Drill Hole	From (ft)	To (ft)	Length (ft)	Gold (oz/t)⁽¹⁾
BH 40-23	147.0	157.0	10.0*	0.102
	205.0	226.0	21.0	0.230
BH 40-24	142.0	173.0	31.0	1.060
BH 40-34	182.0	192.0	10.0*	0.106
BH 40-35	329.5	339.5	10.0*	0.132
BH 40-41	162.0	181.0	19.0	0.280
BH 40-42	224.0	236.0	12.0	0.180
BH 40-43	237.0	249.0	12.0	1.140
BH 40-46	278.0	288.0	10.0*	0.124
	307.0	317.0	10.0*	0.558
	330.0	340.0	10.0*	0.160
BH 40-47	236.0	262.0	26.0	0.260
BH 40-48	197.0	207.0	10.0*	0.174
BH 40-49	234.0	244.0	10.0*	0.106

(1) All values represent either a single interval or were composited using a weighted average based on sample interval length.

* averaged with 0.025 oz/t dilution to reach 10-foot thickness

In 1997, Orvana Minerals used recent and historic drilling data to prepare a report on the Butte Highlands property. The report provided a preliminary technical review of feasibility issues, identifying no fatal flaws to mine development. The report also noted that suitable sites for a mill and tailings pond are present on the property, custom milling at existing nearby facilities was feasible, and access to the deposit could be achieved with a decline from either of two existing portals.

Drilling by Timberline Resources

Four core holes were drilled in 2008 totaling 6,757 feet of drill core. The results were positive, resulting in confirmation and extension of the stratigraphic controlled mineralization to the northwest; and the discovery of an additional zone at depth near the northwest end of the known mineralized extents. The drilling also indicated a potential zone of broader lower grade material within the intrusive which may be amenable to bulk underground mining methods.

In 2009 BHJV completed a five hole core drill program totaling 7,244 feet of drilling. The first three drill holes were drilled to the northwest of the main mineralized body in the hopes of extending mineralization in that area. The first drill hole (BHDDH09-01) encountered mineralization but it appears to be on the outer margins. Two narrow intercepts above 0.1 ounces per ton gold (Au) were encountered. The first was 0.8 feet from 1269.8 feet to 1270.6 feet grading 0.115 ounces per ton Au. The second was 2.5 feet from 1401.1 to 1403.6 feet grading 0.356 ounces per ton Au. The second drill hole (BHDDH09-02) encountered mineralized formation before abruptly intersecting an unexpected fault which removed most of the favorable Wolsey Formation. The third drill hole (BHDDH09-03) encountered the same faulting as in BHDDH09-02 but the entire favorable horizon was removed, consequently no mineralization was encountered in either of the drill holes. The fourth hole (BHDDH09-04) was drilled in the central part of the mineralized area with the intention of infill drilling near known mineralized intercepts. The hole encountered a significant amount of skarn mineralization. Although geologically it appears similar to high grade material, it is lower grade than nearby mineralization. The fifth drill hole (BHDDH09-05) was drilled central to the mineralized area but significantly up dip of the known mineralization. The purpose of this hole was twofold; to supply geotechnical data for the proposed vent raise, and for exploration. Skarn mineralization was encountered although it was lower grade than the down dip zone. One significant intercept of 3.5 feet from 1200.2 feet to 1207.7 feet grading 0.171 opt Au was encountered in the drill hole. When averaged with the next sample, the intercept is 7.8 feet from 1200.2 feet to 1208 feet grading 0.11 ounces per ton Au.

BHJV also initiated a Hydrologic Reverse Circulation Drill program during 2009. The program consisted of five holes completed for a total of 6,695 feet. Data collected during this program was used to model the hydrologic character of the mineralized area.

A seven hole core drilling program was completed during the year ending September, 30 2010. The program had two purposes; one was to infill and expand mineralization within the known area of mineralized material, and the second was to test potential for mineralization to the east, outside the area of known mineralization. Three holes were drilled within the known extents of the mineralized area while four holes

TABLE OF CONTENTS

were drilled outside to the east of the known extents. Two of the holes drilled interior to the known mineralized extents had significant intercepts in them. Hole BHDDH10-02 had a 9.7 foot intercept grading 0.383 ounces per ton gold. This intercept is generally carried by a 1.72 foot intercept grading 0.768 ounces per ton. This drill hole had a couple additional shorter intercepts that with further exploration drilling may lead into additional ore zones. The first one is a 3.3 foot intercept grading 0.113 ounces per ton Au and the second is a 2 foot intercept grading 0.269 ounces per ton Au.

Hole BHDDH10-07 had sixteen intercepts greater than 0.029 ounces per ton gold. The overall intercept was 43.2 feet from 959.8 feet to 1003 feet at an average grade of .819 ounces per ton Au including one intercept from 971.9 feet to 974.1 feet of 2.2 feet grading 15.242 ounces per ton Au. There are other intercepts in the drill hole but all are less than 0.1 ounces per ton Au.

There were no minable width significant intercepts in the outside exploration holes. Several short intercepts and intercepts of anomalous material were encountered but nothing of economic interest. Hole number BHDDH10-03 contained an intercept from 938.5 to 939.9 consisting of 1.4 feet grading 0.185 ounces per ton gold. Hole number BHDDH10-04 also contained a short intercept from 708.9 to 709.6 consisting of 0.7 feet grading 0.179 ounces per ton gold. Both of these intercepts were short zones on the contact between intrusive material and the Meagher formation. Although we did not encounter significant ore zone intercepts, strides in understanding the geology and genesis of the Butte Highlands gold mineralization were achieved.

All above mentioned intercept values were calculated using a sample length, weighted average calculation or represent a single sample interval. The following table represents intercepts of interest during Timberline Resources tenure on the project.

As of September 30, 2010, the Company has incurred exploration costs to date of approximately \$1,600,000. During the 2011 fiscal year, we do not plan to undertake any significant exploration work on the property. The focus at Butte Highlands in fiscal 2011 will be completion of the underground ramp, underground drilling and bulk sampling by our joint venture partner, Highland.

Highlights from Timberline Resources Drilling

Drill Hole	From (ft)	To (ft)	Intercept length (ft)	Gold (oz/t) ⁽¹⁾
BHDDH08-01	1335.6	1337	1.4	0.27
BHDDH08-02	1171.4	1178.6	7.2	0.11
BHDDH08-02	1193.7	1196.3	2.6	0.11
BHDDH08-02	1326	1351	25	0.10
BHDDH08-02	1577.7	1578.5	0.8	0.14
BHDDH08-03	1207	1209	2	0.62
BHDDH08-03	1242	1279	37	0.21
<i>including</i>	<i>1250</i>	<i>1260</i>	<i>10</i>	<i>0.30</i>
<i>including</i>	<i>1272.7</i>	<i>1279</i>	<i>6.3</i>	<i>0.41</i>
BHDDH08-03	1294	1299	5	0.26
BHDDH08-03	1560.2	1569.2	9	0.41
BHDDH08-03	1580	1615	35	0.14
BHDDH09-01	1269.8	1270.6	0.8	0.11
BHDDH09-01	1401.1	1403.6	2.5	0.36
BHDDH09-04	1023.3	1027.3	4	0.10
BHDDH09-05	1182	1185.4	3.4	0.09
BHDDH09-05	1200.2	1208	7.8	0.11
BHDDH10-02	262.3	272	9.7	0.38
BHDDH10-02	300.1	303.4	3.3	0.11
BHDDH10-02	319.4	321.4	2	0.27
BHDDH10-03	938.5	939.9	1.4	0.19
BHDDH10-04	708.9	709.6	0.7	0.20
BHDDH10-07	959.8	1003	43.2	0.82
<i>including</i>	<i>971.9</i>	<i>974.1</i>	<i>2.2</i>	<i>15.24</i>

(1) All values represent either a single interval or were composited using a weighted average based on sample interval length.

Idaho Copper-Silver Property

The Snowstorm Prospect

The Snowstorm Project is located in north Idaho's "Silver Valley" and features the Snowstorm Mine, a historic operation that produced 800,000 tons of ore averaging 4-percent copper and 6 ounces per ton (oz/t) silver. Snowstorm mineralization occurred as disseminated copper and silver found in the same Revett Formation quartzites that host the Troy, Rock Creek, and Montanore deposits on the Montana Copper Sulfide Belt, but was of a much higher grade. The Snowstorm property, which is 2 miles northeast of the Lucky Friday Mine near Mullan in Shoshone County, Idaho, lies in the southwest corner of the Montana Copper Sulfide Belt where it overlaps the northeast corner of the Coeur d'Alene Mining District. Timberline controls 100-percent of the Snowstorm Project.

Exploration work has been conducted in the project area for decades. U.S. Borax conducted a program focusing on the nearby Military Gulch area during the 1980s. Later, Silver Mountain Lead Mines, The Bunker Hill Company, and Hecla held the project area and also conducted significant exploration. Timberline has obtained access to most of this data, which represents hundreds of thousands of dollars worth of work. This data was reviewed and assembled to aid in the development of the 2005 exploration program.

In late-2005, Timberline completed a Phase I exploration program at Snowstorm, designed as an initial evaluation of the potential for copper-silver mineralization in Upper Revett quartzite within the large project area. The program consisted of 10 core holes totaling 4,104 feet, drilled at nine widely-spaced sites along the projected mineralized horizon at depths ranging from 149 to 712 feet.

Mineralization was found to occur within the lower unit of the Upper Revett quartzite, with all ten drill holes encountering the quartzite in thicknesses varying from 37 to 57 feet. Although the continuity of the stratigraphy and the mineralized horizon was demonstrated, bulk grades across the horizon were sub-economic, with copper values typically less than 0.3-percent and silver values typically less than 0.25 oz of silver/ton. Much of the mineralization in the shallower intercepts was oxidized with leaching contributing to the lower grades. In the sulfide zones, chalcopyrite was the predominate sulfide rather than bornite or chalcocite. Results of the drilling were reported in the Company's 8-K report dated January 3, 2006.

Timberline submitted a technical report on the Phase I exploration program at Snowstorm, along with a Phase II exploration proposal, to Hecla as required by an earn-in agreement. Hecla has subsequently elected not to participate in future expenditures at Snowstorm and thus retains a 4-percent net smelter returns (NSR) royalty on any future production from the project. Timberline now controls 100-percent of the Snowstorm prospect.

The mineralized horizon at the Snowstorm Mine was discovered in outcrop and subsequently developed with four adits, each driven at lower elevations to access its nearly vertical structure. The horizon appears to have been offset by a structure near the lowest adit and little systematic exploration has been conducted for this lower portion of the ore body. No stratabound copper-silver deposit has since been discovered that approached the grades of the Snowstorm.

In May 2005, the Company signed a Mineral Lease Agreement with Snowshoe Mining Co. for additional ground adjacent to the Snowstorm project area. The property subject to the Snowshoe Agreement includes the patented claims of Mineral Survey 2224, encompassing an area of approximately 76 acres, just west of the Snowstorm claims. The Agreement calls for an initial payment of \$8,000, with annual payments increasing to \$15,000 by May 2009, and remaining at that level thereafter. The Company will pay a 3-percent NSR royalty on any production from the Snowshoe property, and will perform a minimum of \$10,000 worth of exploration work upon it annually. The work may be performed on or for the benefit of the Snowshoe claims. Hecla previously elected to include the Snowshoe claims within the area of interest, and will consequently receive a 1-percent NSR royalty on any production from the Snowshoe property.

As of September 30, 2010, Timberline does not consider the Snowstorm prospect to be a material property. No material future expenditures are planned on the prospect at this time.

Idaho Gold Property

The Spencer Prospect

The Spencer prospect covers 640 acres on the western end of the Kilgore-Spencer Trend, a northeast-trending belt of rhyolite volcanics known to host epithermal gold-silver mineralization, just south of a privately-held opal mine about nine miles northeast of near the town of Spencer, Idaho. The Company believes that the property has the potential to host both open-pit and underground gold deposits.

The geochemistry at Spencer is consistent with the upper levels of an epithermal system. Although there was considerable interest in the region during the 1980s and 1990s, the Spencer property has never been drill tested.

The Company has performed a phase-one exploration program consisting of reconnaissance-scale geological mapping along with rock chip and soil geochemical sampling. Future work may include more detailed mapping and sampling, and possibly a geophysical survey to help define drill targets.

The Spencer Prospect is held by State of Idaho Department of Lands Mineral Lease No. 9347. The Mineral Lease was issued to a prior Director of Timberline, who assigned it to the Company for consideration of common stock and approximately \$3,000 in expenses.

TABLE OF CONTENTS

The prospect is located in Section 16, Township 12 North, Range 37 East, in Clark County, Idaho. The lease covers an area of approximately 640 acres and calls for annual payments to the State of Idaho of \$640. Royalties on production of previous metals are 5-percent of the gross receipts from the sale of minerals produced, less reasonable transportation, smelting and treatment costs.

As of September 30, 2010, Timberline does not consider the Spenser prospect to be a material property. No future expenditures are planned on the prospect at this time.

Montana Copper-Silver Properties

The Minton Pass, East Bull, Standard Creek, Lucky Luke, Clear Peak and Copper Rock Prospects

In 2004, Timberline acquired four properties on the Montana Copper Sulfide Belt in Lincoln and Sanders counties. All four properties are interpreted as sediment-hosted copper-silver occurrences located in the Revett Formation of the Montana Copper-Silver Belt and are considered early-stage exploration prospects. The properties were held by U.S. Borax and its successor company, Kennecott Exploration, during the 1980s and early-1990s. Timberline has acquired the mapping and sampling data from the U.S. Borax program. There has been no documented activity in these areas since 1992.

In the 1970s and 1980s, major exploration companies identified several copper-silver occurrences within the Montana Copper Sulfide Belt, and successfully outlined three world-class ore bodies, including Troy, Rock Creek and Montanore. These quartzite-hosted deposits are characterized by their lateral extensive size and continuity of mineralization.

Metasedimentary rocks of the Precambrian Belt Supergroup underlie the area. Outcropping rocks consist of a sequence of argillites, siltstones, and quartzites representing the basal portion of the Wallace, St. Regis, and Revett formations, along with the upper portion of the Burke Formation. Locally, these rocks strike northwest with a shallow westerly dip. Major faulting associated with the mineralization is generally north-northwest. Disseminated bornite with secondary chrysocolla and malachite is reported to occur within a specific quartzite horizon of the Revett Formation.

In 2008, Timberline acquired two additional prospects in the same favorable mineralized geology, Clear Peak and Copper Rock. These properties have the same geologic description as the properties described above. Both Clear Peak and Copper Rock were previously explored by Asarco Exploration Company, Inc.

All claims were staked by Timberline and are not subject to any underlying production royalty. All of these claims have been filed with the BLM.

The State of Montana has banned the use of cyanide in mining activities within the state. Cyanide is used in the mining of gold. Since Timberline's Montana prospects are for silver and copper only, this ban does not affect our plans for this property in Montana.

As of September 30, 2010, Timberline does not consider any of the Minton Pass, East Bull, Standard Creek, Lucky Luke, Clear Peak or Copper Rock prospects to be material properties. No future expenditures are planned on the prospects at this time.

Overview of Regulatory, Economic and Environmental Issues

Hard rock mining and drilling in the United States is a closely regulated industrial activity. Mining and drilling operations are subject to review and approval by a wide variety of agencies at the federal, state and local level. Each level of government requires applications for permits to conduct operations. The approval process always involves consideration of many issues including but not limited to air pollution, water use and discharge, noise issues, and wildlife impacts. Mining operations always involve preparation of an environmental impact statement that examines the probable effect of the proposed site development. Federal agencies that may be involved include: The U.S. Forest Service (USFS), Bureau of Land Management (BLM), Environmental Protection Agency (EPA), National Institute for Occupational Safety and Health (NIOSH), the Mine Safety and Health Administration (MSHA) and the Fish and Wildlife Service (FWS). Individual states also have various environmental regulatory bodies, such as Departments of Ecology and so on. Local authorities, usually counties, also have control over mining activity. An example of such regulation is the State of Montana's recent ban on the use of cyanide in mining activities within the state. Cyanide is used in the mining of gold. However, since some of our prospects in Montana are for silver and copper this ban does not affect those properties. Our Butte Highlands project in Montana is partially on patented ground and is an underground gold prospect. It is anticipated that any production from this property would be shipped to nearby mills for processing as opposed to building our own mills and processing facilities, thus this ban would not affect our plans in Montana. The Elkhorn project is nearby and similar to Butte Highlands and is following a similar plan with public support. We are not aware of any other states that plan to enact similar legislation.

Gold, silver and copper are mined in a wide variety of ways, both in open pit and underground mines. Open pit mines require the gold deposit to be relatively close to the surface. These deposits tend to be low grade (such as 0.01-0.03 ounces per ton gold) and are mined using large, costly earth moving equipment, usually at very high tonnages per day.

Open pit operations for gold usually involve heap leaching as a metallurgical method to remove the gold. Heap leaching involves stacking the ore on pads which are lined with an impenetrable surface, then sprinkling the gold with a weak cyanide solution to extract the gold. The particle impregnated solution is collected and the gold recovered through further processing.

TABLE OF CONTENTS

Underground metal mines generally involve higher grade ore bodies. Less tonnage is mined underground, and generally the higher grade ore is processed in a mill or other refining facility. This process results in the accumulation of waste by-products from the washing of the ground ore. Mills require associated tailings ponds to capture waste by-products and treat water used in the milling process.

Capital costs for mine, mill and tailings pond construction can easily run into the hundreds of millions of dollars. These costs are factored into the profitability of a mining operation. Metal mining is sensitive to both cost considerations and to the value of the metal produced. Metals prices are set on a world-wide market and are not controlled by the operators of the mine. Changes in currency values or exchange rates can also impact metals prices. Thus changes in metals prices or operating costs can have a huge impact on the economic viability of a mining operation.

Environmental protection and remediation is an increasingly important part of mineral economics. In some cases, particularly in Montana, with its concern for its grizzly bear population, mining companies have been required to acquire and donate additional land to serve as a substitute habitat for this endangered species.

Estimated future costs of reclamation or restoration of mined land are based principally on legal and regulatory requirements. Reclamation of affected areas after mining operations may cost millions of dollars. Often governmental permitting agencies are requiring multi-million dollar bonds from mining companies prior to granting permits, to insure that reclamation takes place. All environmental mitigation tends to decrease profitability of the mining operation, but these expenses are recognized as a cost of doing business by modern mining and exploration companies.

Mining and exploration activities are subject to various laws and regulations governing the protection of the environment. These laws and regulations are continually changing and are generally becoming more restrictive. We conduct our operations so as to protect the public health and environment and believe our operations are in compliance with applicable laws and regulations in all material respects. We have made, and expect to make in the future, expenditures to comply with such laws and regulations, but cannot predict the full amount of such future expenditures.

Every mining activity has an environmental impact. In order for a proposed mining project to be granted the required governmental permits, mining companies are required to present proposed plans for mitigating this impact. In the United States, where our properties are located, no mine can operate without obtaining a number of permits. These permits address the social, economic, and environmental impacts of the operation and include numerous opportunities for public involvement and comment.

We intend to focus on exploration and discovery of mineral resources, not their production. If we are successful, the ore bodies discovered will be attractive to production companies. The mining industry is, like agriculture, a fundamental component of modern industrial society, and minerals of all sorts are needed to maintain our way of life. If we are successful in finding an attractive ore body, be it gold, silver or copper, sufficient value will be created to reward the Company's shareholders and allow for all production and reclamation expenses to be paid by the actual producer to whom we convey, assign or joint venture the project.

ITEM 3. LEGAL PROCEEDINGS

In January 2009, the Company filed a complaint in the United States District Court for the District of Idaho (the "Court") against American Drilling, LLC, American Drilling Corporation (along with American Drilling, LLC referred to as "American Drilling"), and Steven Elloway ("Elloway"). Timberline Drilling alleged that when Elloway resigned his employment with the Company, he immediately started American Drilling, and that Elloway and American Drilling had subsequently violated Elloway's Supplemental Income Agreement with Timberline Drilling, which restricted his post-termination competitive activities. In addition to seeking monetary damages, Timberline Drilling asked the Court to issue an injunction to prohibit future improper competition or use of Timberline Drilling trade secrets by Elloway or American Drilling.

In July, 2010, the parties entered into a mutual settlement and release whereby Elloway and American Drilling agreed to pay Timberline \$150,000 in exchange for releasing Elloway and American Drilling from the complaint. The parties also mutually agreed to releases from any future litigation by all parties. The payment was made to Timberline in August 2010.

No director, officer or affiliate of Timberline and no owner of record or beneficial owner of more than 5.0% of our securities or any associate of any such director, officer or security holder is a party adverse to Timberline or has a material interest adverse to Timberline in reference to pending litigation.

ITEM 4. [REMOVED AND RESERVED]

PART II

ITEM 5. MARKET FOR COMMON EQUITY, RELATED STOCKHOLDER MATTERS, AND ISSUER PURCHASES OF EQUITY SECURITIES

Market Information

Our common stock is listed on the NYSE Amex and is quoted under the trading symbol “TLR”. On June 3, 2010, the Company’s common stock also began trading on the TSX Venture Exchange (“TSX-V”) in Canada and is quoted under the trading symbol “TBR”. The high and low sale prices for our common stock as quoted on the NYSE Amex and the TSX-V were as follows:

Period ⁽¹⁾	NYSE Amex (US\$)		TSX-V (Cdn\$)	
	High	Low	High	Low
2010				
First Quarter	\$1.47	\$0.81	— ⁽²⁾	— ⁽²⁾
Second Quarter ⁽²⁾	\$1.41	\$0.89	\$1.10	\$0.90
Third Quarter	\$1.25	\$0.73	\$1.45	\$0.79
Fourth Quarter ⁽³⁾	\$1.40	\$1.02	\$1.44	\$1.01
2009				
First Quarter	\$1.50	\$0.19	— ⁽²⁾	— ⁽²⁾
Second Quarter	\$0.53	\$0.22	— ⁽²⁾	— ⁽²⁾
Third Quarter	\$0.87	\$0.31	— ⁽²⁾	— ⁽²⁾
Fourth Quarter	\$1.68	\$0.67	— ⁽²⁾	— ⁽²⁾
2008				
Fourth Quarter	\$1.50	\$0.23	— ⁽²⁾	— ⁽²⁾

(1) Quarters indicate calendar year quarters.

(2) Our common stock began trading on the TSX-V on June 3, 2010

(3) Through December 15, 2010

On December 15, 2010, the closing sale price for our common stock was \$1.02 on the NYSE Amex and \$1.02 Cdn. on the TSX-V.

As of December 15, 2010, we had 55,792,938 shares of common stock issued and outstanding, held by approximately 760 registered shareholders. In many cases, shares are registered through intermediaries, making the precise number of shareholders difficult to obtain.

On May 27, 2010, the Company received notification from the NYSE Amex that Timberline had resolved its continued listing deficiencies relating to a notice received on February 13, 2009, such that a compliance period which had been accepted by the NYSE Amex had ended. The Company must maintain compliance with the continued listing standards in the future or risk being subject to delisting procedures again. If we are unable to maintain our listing on the NYSE Amex and are unable to obtain a comparable listing, the liquidity of our common stock could decrease significantly and our ability to raise additional capital through equity or convertible debt could be impaired.

Dividend Policy

We anticipate that we will retain any earnings to support operations and to finance the growth and development of our business. Therefore, we do not expect to pay cash dividends in the foreseeable future. Any further determination to pay cash dividends will be at the discretion of our board of directors and will be dependent on the financial condition, operating results, capital requirements and other factors that our board deems relevant. We have never declared a dividend.

Purchases of Equity Securities by the Issuer and Affiliates

There were no purchases of our equity securities by us or any of our affiliates during the year ended September 30, 2010.

Stock Incentive Plans

In February 2005, our Board adopted the 2005 Stock Incentive Plan which was approved by a vote of shareholders at our Annual Meeting of Shareholders on September 23, 2005. This plan authorizes the granting of up to 750,000 non-qualified stock options to Officers, Directors, and consultants.

On August 31, 2006, our Board of Directors approved an amendment to the Timberline Resources Corporation 2005 Equity Incentive Plan (the “Amended 2005 Plan”) for the purposes of increasing the total number of shares of common stock that may be issued pursuant to Awards granted under the original 2005 Plan from 750,000 shares to 2,750,000 shares and allowing “Ten Percent Shareholders” (as defined

[TABLE OF CONTENTS](#)

in the Amended 2005 Plan) to participate in the plan on the same basis of any other participant. The Amended Plan was approved by a vote of shareholders at our Annual Meeting of Shareholders on September 22, 2006.

On August 22, 2008, our shareholders approved a proposal for the increase in the total number of shares of common stock that may be issued pursuant to awards granted under the original 2005 Plan as previously amended. Following the increase, the plan provides for 7,000,000 shares of common stock for awards under the plan.

On May 28, 2010, our shareholders approved a proposal for the increase in the total number of shares of common stock that may be issued pursuant to awards granted under the original 2005 Plan as previously amended. Following the increase, the plan provides for 10,000,000 shares of common stock for awards under the plan.

Equity Compensation Plans

The following summary information is presented as of September 30, 2010.

	Number of securities to be issued upon exercise of outstanding options, warrants, and rights (a)	Weighted-average exercise price of outstanding options, warrants, and rights (b)	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c)
Equity compensation plans approved by security holders ⁽¹⁾	6,203,641 ⁽¹⁾	\$0.96	1,769,689
Equity compensation plans not approved by security holders			
TOTAL	6,203,641 ⁽¹⁾	\$0.96	1,769,689

(1) See “Stock Incentive Plans”, above.

As to the options granted to date, there were 1,277,003 options exercised during the year ended September 30, 2010. For the year ended September 30, 2009, 75,000 options were exercised.

Sale of Unregistered Securities

During the year ended September 30, 2010, all transactions in which we have offered and sold unregistered securities pursuant to exemptions under the Securities Act of 1933, as amended, have been previously reported on Current Reports on Form 8-K.

ITEM 6. SELECTED FINANCIAL DATA

Not Applicable.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATION

You should read the following discussion and analysis of our financial condition and results of operations together with our financial statements and related notes appearing elsewhere in this report. This discussion and analysis contains forward-looking statements that involve risks, uncertainties and assumptions. Our actual results may differ materially from those anticipated in these forward-looking statements as a result of many factors, including, but not limited to, those set forth under “Risk Factors and Uncertainties” and elsewhere in this document.

Overview

We commenced our exploration stage in January 2004 with the change in the management of the Company. From January 2004 until March 2006, we were strictly a mineral exploration company. Beginning with the management appointments of John Swallow and Paul Dirksen, the addition of Randal Hardy, our acquisition of a drilling services company, the acquisition of Butte Highlands, and the acquisition of Staccato Gold Resources Ltd., we continue to advance our business plan. Prior to our new business model, the addition of new management, the purchase of Timberline Drilling (formerly known as Kettle Drilling), and a more active and focused exploration division, the Company had no reported revenues and accumulated losses.

TABLE OF CONTENTS

We achieved significant milestones during 2010. Our acquisition of Staccato Gold Resources Ltd. and its South Eureka Property in Nevada's Battle Mountain – Eureka gold trend, which includes the Lookout Mountain Project, added an advanced-stage exploration project and other earlier stage exploration opportunities to our portfolio. We have commenced a significant and focused exploration campaign at South Eureka, and we expect to announce an updated gold mineralization estimate in fiscal year 2011.

Our Butte Highlands Joint Venture in Montana continued to make progress during the 2010 fiscal year. The joint venture completed all surface facilities and advanced the underground ramp to the top of the expected mineralization, and we continue to move forward with the remaining underground mine development and permitting activities. Underground definition drilling began subsequent to our fiscal year end, and we anticipate commencement of gold production in early Q1 2012.

Our drilling services subsidiary, Timberline Drilling, was very successful in the United States during 2010, earning approximately \$1.7 million in net income in FY2010 and a solid gross margin of 21%. Timberline Drilling also extended its drilling contract with Newmont into 2014 and added other clients with long-term mining projects. We made the decision late in the year to discontinue operations at our Mexican drilling services subsidiary, WWE, and we redeployed WWE's drilling assets to the United States for potential use by Timberline Drilling.

Drilling Services

Timberline Drilling provides both surface and underground drilling services, with its largest client being Newmont Mining. Timberline Drilling specializes in underground, hard rock core drilling – a niche business that we believe is well-positioned as the industry continues to mature and exploration projects are advanced into producing mines. Our underground focus has provided a solid base of operations during times when a large percentage of the above-ground and more speculative exploration drilling has been cut back and/or delayed due to economic conditions.

In prior fiscal years there was a significant liability on the Company's balance sheet related to interest and penalties for late payment of payroll taxes for payrolls during the period from October 1, 2007 through May 15, 2008. This liability was generated during a period of substantial company growth when Timberline Drilling's previous management team used available funds to pay other liabilities of the subsidiary rather than paying the payroll taxes and resulting penalties and interest. The Company repaid all outstanding payroll taxes owing from these periods during the year ending September 30, 2009, and repaid all related IRS penalties and interest during the year ended September 30, 2010. As a result, the IRS has released all liens against Timberline Drilling, and there are no longer any liabilities on the Company's balance sheet related to unpaid payroll taxes, penalties, or interest. The Company has made timely payments on all payroll taxes since May 15, 2008.

During the year ended September 30, 2010, due to declining operational and financial results, we decided to cease the operations of Timberline Drilling's wholly-owned Mexican subsidiary, WWE. WWE's drill rigs and related assets were moved back to the U.S. where they are available for use by Timberline Drilling.

Revenue at Timberline Drilling increased considerably during the past year as a result of increased drilling activity in the United States. The increased drilling activity occurred primarily due to renewed availability of exploration and development capital, improvements in the global economy and higher prices for both gold and silver. Our management team has continued to focus its efforts throughout the past year on managing our expenses in relation to our current rates of revenue to assure sustainable profitability from our drilling entity. While we still believe additional improvements can be made, Timberline Drilling has now achieved six consecutive quarters of profitability.

For fiscal year 2011, we expect demand for our drilling services to increase compared to the prior year, with a corresponding increase in the utilization of our drilling rigs. We expect to generate moderate revenue growth with our largest customer, our other customers, and new customers as we continue to develop relationships and demonstrate excellent performance. We intend to continue to streamline the operations and carefully manage costs in order to generate greater profitability and provide positive cash flow to the parent company. Safety will remain a priority as we expect to continue to operate with no lost-time accidents and to reduce the number of incidents.

Mineral Exploration

As noted above, in June, 2010, the Company acquired Staccato Gold Resources Ltd. and its South Eureka Property in the Nevada's Battle Mountain – Eureka gold trend, which includes the Lookout Mountain Project, and is one of the largest undeveloped exploration properties in Nevada, encompassing some 23 square miles. Since our acquisition of Staccato, we commenced an aggressive \$2,500,000 work program on the South Eureka property. The program objective was designed to obtain sufficient data to complete an updated mineralization estimate, conduct metallurgical studies and tests, and detail map the geology of the property to better understand the controls of mineralization and to outline additional exploration drill targets for testing in 2011. The information generated by this program is expected to be incorporated into a preliminary economic assessment during the year ended September 30, 2011.

As of September 30, 2010 Timberline is on schedule at Lookout Mountain, with one Timberline Drilling core rig and two RC rigs operating on site. The metallurgical scoping study has been formalized, and geologic mapping is on-going. All drilling and geologic mapping will be completed by December 31, 2010, and metallurgical testing commenced in November 2010.

At Butte Highlands, a seven hole core drilling program was completed during the year ending September, 30 2010. The program had two purposes; one was to infill and expand mineralization within the known area of mineralized material, and the second was to test potential for mineralization to the east, outside the area of known mineralization. Three holes were drilled within the known extents of the mineralized

TABLE OF CONTENTS

area while four holes were drilled outside to the east of the known extents. Although we did not encounter significant ore zone intercepts, strides in understanding the geology and genesis of the Butte Highlands gold mineralization were achieved.

Timberline is being carried to production and is a 50% joint venture partner in the Butte Highlands Joint Venture. Underground development continues on the project, with underground definition drilling commencing subsequent to September 30, 2010. For the remainder of 2010 and early 2011, work is to continue on up to 6,700 feet of underground ramps, 60,000 feet of underground core and RC drilling, and a 10,000-ton bulk sample, all of which is being funded by the Company's joint venture partner.

The required application has been submitted for a Hard Rock Operating permit at Butte Highlands, and work is continuing on the other associated permits required for the operation. No material permitting obstacles are expected as the project advances toward targeted production. Surface facilities and infrastructure required for development and production are already in place under the Company's exploration permit which has been in place since August 2009.

Butte Highlands is expecting to produce gold commencing in early Q1 2012, with the Company's share expected to be approximately 30,000 ounces of gold per annum over the projected mine life of ten years based upon the preliminary internal operations plan for Butte Highlands. All mine plan information is based on Company internal analysis such that detailed figures are non 43-101 compliant. As part of the current program of work, the Company intends to prepare and file a NI 43-101 Report by the end of June, 2011.

Timberline's Butte Highlands Joint Venture is the first example of the Company's strategy to enter into creative structures that move production responsibility to other parties while allowing exposure to gold production, where financing has been provided by a third party with proven expertise in underground mine development and operation. This has been achieved with no dilution to Timberline shareholders. As noted, all expenditures relating to the development of the projected underground mine are being paid by Timberline's joint venture partner, with a total expected development budget of USD \$17 million.

Our management and geologists remain committed to providing exploration and potential for discovery to our investors. Looking ahead, it is the opinion of management that our primary commodity focus should be on gold, and to a lesser extent on silver in the precious metals area. Furthermore, we believe that projects similar to Lookout Mountain and Butte Highlands are a good fit for the current environment and the unique qualifications of our people, drilling subsidiaries and strategic partners.

Results of Operations for Years Ended September 30, 2010 and 2009

Consolidated Results

(\$US)	Year Ended September 30	
	2010	2009
Revenue	\$20,733,337	\$13,242,093
Gross profit	4,371,810	1,092,575
Net income (loss) from continuing operations:		
Timberline Corporate/Exploration	(5,843,114)	(5,997,234)
Timberline Drilling	1,709,938	(1,132,262)
Consolidated net loss from continuing operations	(4,133,176)	(7,129,496)
Loss from discontinued operations, net of tax	(1,617,652)	(179,132)
Consolidated net loss	\$(5,750,828)	\$(7,308,628)

Our revenues are derived entirely from our drilling subsidiary. Our revenue increase from the previous year was primarily due to an increase in the number of drill rigs in service during the year. The improvement in gross profits compared to the prior year is a function of productivity improvements which have led to higher revenues per foot drilled and higher average footage drilled by each operating drill rig, the implementation of processes and controls that have reduced operating costs, and improved retention of skilled labor.

Our overall consolidated net loss for the year decreased in comparison to the prior year primarily as a result of a greater than \$3 million improvement in net income from Timberline Drilling and a reduction in salaries, benefits and professional expenses, offset by a nearly \$2 million increase in mineral exploration expenses by the Company.

Timberline Corporate and Exploration Division

(\$US)	Year Ended September 30	
	2010	2009
Exploration expenses:		
Butte Highlands	\$ 590,555	\$ 60,797
South Eureka/Lookout Mountain	1,156,137	-
Other exploration properties	474,570	432,592
Total exploration expenditures	2,221,262	493,389
Non cash expenses:		
Stock option and stock issuance expense	1,468,074	2,234,856
Depreciation, amortization and accretion	59,861	36,492
Total non cash expenses	1,527,935	2,271,348
Professional fees expense	927,535	1,278,573
Interest expense	556,625	761,469
Interest and other income	(193,420)	(16,166)
Other general and administrative expenses	1,211,208	1,208,621
Income tax benefit	(408,031)	-
Net loss – Timberline Corporate and Exploration	\$ (5,843,114)	\$ (5,997,234)

The decrease in the after tax net loss for Timberline Corporate and the Exploration division for the year ended September 30, 2010 as compared to the previous year's after tax net loss is primarily a result of lower stock option expenses, reduced legal and accounting costs, lower interest expense and realization of an income tax benefit, offset by significantly increased expenditures on mineral exploration activities at our Butte Highlands and South Eureka/Lookout Mountain properties. The income tax benefit during the year ended September 30, 2010 arose as a result of a reduction in deferred income tax liabilities assumed upon the acquisition of Staccato Gold Resources Ltd.

Exploration expenses increased significantly from the previous year as a result of exploration drilling undertaken in 2010 at our Butte Highlands property, as well as our acquisition of the South Eureka/Lookout Mountain property in June 2010. Non cash expenses decreased significantly in 2010 compared to the prior year as a result of a reduced value of stock options vesting during the current year.

Timberline Drilling

(\$US)	Year Ended September 30	
	2010	2009
Total revenue	\$ 21,813,435	\$ 13,242,093
Less elimination of intersegment revenues	(1,080,098)	-
Revenue	\$ 20,733,337	\$ 13,242,093
Gross profit	4,371,810	1,092,575
General and administrative expenses	2,545,256	1,696,934
Interest and other expense, net	116,616	527,903
Net income (loss)	\$ 1,709,938	\$ (1,132,262)

Timberline Drilling's increase in revenue is attributable to a significantly higher utilization rate of our drill rigs, primarily due to our major customer increasing the number of drills required and an increase in exploration drilling. Overall the demand for drilling services appears to have stabilized during the past year. Junior resource and exploration stage companies are gaining access to capital for their drilling programs, and, as a result, the overall demand for drilling services, while not as robust as in 2007 and 2008, continues to show signs of improvement. Timberline Drilling has secured several new contracts with exploration stage companies. The improvement in gross profits compared to the prior year is a function of productivity improvements which have led to higher revenues per foot drilled and higher average footage drilled by each operating drill rig, the implementation of processes and controls that have reduced operating costs, and improved retention of skilled labor.

Increased year over year general and administrative expenses at Timberline Drilling reflect an expected increase in overhead costs to support the increased number of operating drill rigs as compared to the previous year. The general and administrative expenses for the year ended September 30, 2009 also included a \$350,000 recovery of severance expenses accrued in the prior year. Interest and other expenses decreased considerably in the year ending September 30, 2010 compared to the prior year, as the Company incurred IRS interest charges on unpaid payroll taxes in the prior year.

Discontinued Operations – WWE

(\$US)	Year Ended September 30	
	2010	2009
Revenues	\$ 1,978,270	\$ 4,331,005
Cost of revenues	(2,850,142)	(3,879,272)
Operating expenses	(428,549)	(698,016)
Provision for closed operations	(468,598)	-
Foreign exchange gain (loss)	142,654	(74,779)
Interest income	4,069	17,601
Interest expense	(1,265)	(20,760)
Other income	5,909	-
Income tax expense	-	(145,089)
Loss from discontinued operations, net of tax	\$ (1,617,652)	\$ (179,132)

During the year ended September 30, 2010, due to declining operational and financial results, we decided to cease the operations of Timberline Drilling's wholly-owned Mexican subsidiary, WWE. WWE's drill rigs and related assets were moved back to the U.S. where they are available for use by Timberline Drilling.

Financial Condition and Liquidity

At September 30, 2010, we had assets of \$31,268,529 consisting of cash in the amount of \$4,638,674; restricted cash of \$379,952; accounts receivable in the amount of \$908,358; materials and supplies inventory valued at \$1,238,369; property, mineral rights, and equipment, net of depreciation of \$19,261,510; goodwill related to the acquisition of Timberline Drilling in the amount of \$2,808,524; and other assets of \$2,033,142.

Disruptions in the current credit and financial markets have had a significant material adverse impact on a number of financial institutions and have limited access to capital and credit for many companies. While access to capital has improved recently, these disruptions could, among other things, make it more difficult for us to obtain, or increase our cost of obtaining, capital and financing for our operations. Our access to additional capital may not be available on terms acceptable to us or at all.

We expect to rely upon the revenues generated by our contract core drilling services subsidiary. While the recent economic instability makes it difficult for the Company's management to accurately predict revenues from these services into the 2011 fiscal year, management expects that if commodity prices for gold and silver remain at or near the levels seen in fiscal 2010 that our revenues will increase in step with increased demand for drilling services by both our current customers as well as new customers. While we expect cash flows from our contract core drilling services subsidiary to increase in fiscal 2011 if our revenues increase, if cash flows decline or are insufficient to fund our expenditures, our discretionary exploration activities and other operations will either be curtailed significantly or we will be reliant upon equity financings to continue our exploration activities into the future. The current market conditions could make it difficult or impossible for us to raise necessary funds to meet our capital requirements. If we are unable to obtain financing through equity investments, we will seek multiple solutions including, but not limited to, asset sales, credit facilities or debenture issuances.

At September 30, 2010 the Company has working capital of \$2,826,737, compared to working capital of \$169,452 at September 30, 2009. Management expects to continue to maintain or increase the amount of working capital via continued improvements in operating cash flows at the Company's drilling subsidiary, monitoring discretionary exploration expenditures, reducing professional and consulting expenses, and potentially obtaining financing through equity investments. Management expects to maintain or improve operating cash flows at the Company's drilling subsidiary by increasing the utilization rate of our drills and closely managing payroll expenses, supplies inventory levels, and general and administrative costs. We plan to continue exploration programs on our material exploration properties, to fund some exploratory activities and drilling on early-stage properties, and to seek additional acquisition opportunities.

During the year ended September 30, 2010, due to declining operational and financial results, we decided to cease the operations of Timberline Drilling's wholly-owned Mexican contract core drilling subsidiary, World Wide Exploration. For additional information regarding the operating, investing and financing cash flows associated with our discontinued operations, please refer to Note 16 to the Company's consolidated financial statements contained in Item 8 of this Annual Report. The closure of our Mexican operations is not expected to have a material impact on the Company's cash flows in future periods.

As a result of our current cash balance, improved performance of our drilling subsidiary and our ability to curtail discretionary exploration expenditures as needed, management believes that it has sufficient working capital to meet the Company's ongoing operating expenses for the next 12 months. Additional financing may be required if the Company seeks to undertake further property acquisitions or expand its exploration or drilling services operations.

TABLE OF CONTENTS

Financing activities

In October 2009, warrants to purchase 1,085,944 common shares of the Company were exercised by warrant holders at a price of \$0.50 per common share, for aggregate total proceeds of \$542,972. Proceeds from the warrant exercises were used for general working capital and to evaluate merger and acquisition opportunities in mining services and exploration.

In November 2009, the Company initiated a private placement of the Company's restricted common stock. Under the private placement subscription agreement, the Company could sell up to 3,000,000 units for a total of \$3,000,000. The Company reserved the right to increase the amount of the offering in the event that the offering was oversubscribed. Each unit consisted of one share of common stock and one half of one Class A Warrant; with each whole warrant exercisable to acquire one additional share of common stock at an exercise price of \$1.50 per share until May 31, 2010 and thereafter at an exercise price of \$1.75 per share until March 25, 2011. No registration rights were granted for the shares of common stock or the shares of common stock underlying the warrants. The units were sold for \$1.00 each, representing management's estimate of the fair value of the unit. The Company sold a total of 3,003,400 units for gross proceeds of \$3,003,400; with the private placement closing on November 23, 2009. Proceeds from the private placement were used for general working capital and to evaluate merger and acquisition opportunities in mining services and exploration.

On October 31, 2008 the Company entered into a convertible note with Small Mine Development ("SMD"), a company owned by Ron Guill, a director of the Company. The convertible note has a principal amount of \$5.0 million and is collateralized by a pledge of all of the stock of Timberline Drilling, Inc., as well as a Deed of Trust covering the Company's Butte Highlands property in Silver Bow County, Montana (the "Butte Highlands Property").

The convertible note bears interest at 10% annually, compounded monthly, with interest payments due at maturity on October 31, 2010. The convertible note, including accrued interest, is convertible into common stock by SMD at any time prior to payment of the note in full, at a conversion price of \$1.50 per share. Should the Company issue any form of equity security other than the Company's common stock, SMD may also convert all or any portion of the outstanding amount under the Convertible Term Note into the new form of equity security at the issuance price of the new form of equity security. The convertible note may be prepaid in whole or in part at any time without premium or penalty. If the Company defaults on the convertible note, SMD may declare the convertible note immediately due and payable, and the Company must pay SMD an origination fee in the amount of \$50,000.

In June 2010, SMD agreed to extend the maturity date of the convertible note to on or before April 30, 2012. All interest accrued through June 30, 2010 was paid by the Company to SMD at that time. The Company also paid a \$50,000 extension fee to SMD in consideration for the extension of the convertible note. The convertible note was also amended to require interest accrued subsequent to June 30, 2010 to be paid by the Company to SMD monthly, rather than accruing interest to maturity. All other terms of the loan were unchanged.

Under the Right of First Refusal, the Company granted SMD a right of first refusal to purchase the Butte Highlands Property on the same terms as those of any bona fide offer from a third-party upon 60 days' notice from the Company of any such offer. In addition, the Company granted SMD a right to develop the Butte Highlands Property on the same terms as those of any bona fide offer to develop the property from a third-party upon 60 days' notice from the Company of any such offer.

Off-Balance Sheet Arrangements

We do not have any off balance sheet arrangements that are reasonably likely to have a current or future effect on our financial condition, revenues, results of operations, liquidity or capital expenditures.

Critical Accounting Policies and Estimates

See Note 2 to the Company's consolidated financial statements contained in Item 8 of this Annual Report for a complete summary of the significant accounting policies used in the presentation of our financial statements. As described in Note 2, we are required to make estimates and assumptions that affect the reported amounts and related disclosures of assets, liabilities, revenue and expenses. We believe that our most critical accounting estimates are related to asset impairments, asset retirement obligations, and inventory net realizable value.

Our critical accounting policies and estimates are as follows:

Asset Impairments

Significant property acquisition payments for active exploration properties are capitalized. The evaluation of our mineral properties for impairment is based on market conditions for minerals, underlying mineralized material associated with the properties, and future costs that may be required for ultimate realization through mining operations or by sale. If no mineable ore body is discovered, or market conditions for minerals deteriorate, there is the potential for a material adjustment to the value assigned to mineral properties.

The Company reviews the carrying value of equipment for impairment whenever events and circumstances indicate that the carrying value of an asset may not be recoverable from the estimated future cash flows expected to result from its use and eventual disposition. In cases where undiscounted expected future cash flows are less than the carrying value, an impairment loss is recognized equal to an amount by which the carrying value exceeds the fair value of the asset. The factors considered by management in performing this assessment include current operating results, trends and prospects, the manner in which the equipment is used, and the effects of obsolescence, demand, competition, and other economic factors.

Asset Retirement Obligations

The Company has an obligation to reclaim its properties after the surface has been disturbed by exploration methods at the site. As a result we have recorded a liability for the fair value of the reclamation costs we expects to incur in association with our joint venture at the Butte Highlands Gold Project. The Company estimated applicable inflation and credit-adjusted risk-free rates as well as expected reclamation time frames. To the extent that the estimated reclamation costs change, such changes will impact future reclamation expense recorded. A liability is recognized for the present value of estimated environmental remediation (asset retirement obligation) in the period in which the liability is incurred if a reasonable estimate of fair value can be made. The offsetting balance is charged to the related long-lived asset. Adjustments are made to the liability for changes resulting from passage of time and changes to either the timing or amount of the original present value estimate underlying the obligation.

Materials and Supplies Inventory

Inventories consist primarily of parts, operating supplies, drill rods and drill bits. The Company values its materials and supplies inventory, with the exception of drill rods, at the lower of average cost or market. Drill rods are valued using their average cost less an allowance for rod usage on a per-foot drilled basis. The Company reviews the carrying value of inventory for impairment whenever events and circumstances indicate that materials and supplies inventory may no longer be of use by the Company's drilling operation. The Company also periodically assesses the per foot allowance for drill rod usage by assessing the net carrying value of rod inventory relative to the operating condition of rod inventory held by the Company. Allowances are recorded for inventory considered to be in excess or obsolete.

Recently Issued Accounting Standards

In May 2009, the ASC guidance for subsequent events was updated to establish general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued. This statement is effective for interim and annual periods ending after June 15, 2009. Accordingly, the Company adopted the updated guidance in its quarter ending June 30, 2009. The adoption of this statement did not have a material effect on the Company's consolidated financial statements.

In June 2009, the ASC guidance for consolidation accounting was updated to require an analysis to determine whether a variable interest gives the entity a controlling financial interest in a variable interest entity. This statement requires an ongoing reassessment and eliminates the quantitative approach previously required for determining whether an entity is the primary beneficiary. This statement is effective for fiscal years beginning after Nov. 15, 2009. Accordingly, the Company will adopt this updated guidance in fiscal year 2011 and is currently evaluating the impact of adopting this guidance on the consolidated financial statements.

In January 2010, the ASC guidance for fair value measurements was updated to require additional disclosures related to movements of assets among Levels 1 and 2 of the three-tier fair value hierarchy. Also, a reconciliation of purchases, sales, issuance, and settlements of anything valued with a Level 3 method is required. Disclosure regarding fair value measurements for each class of assets and liabilities will be required. The updated guidance was adopted by the Company in its quarter ending December 31, 2009, except for disclosures about the activity in Level 3 fair value measurements which are effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years. Adoption of this updated guidance did not have a material impact on the Company's consolidated financial statements.

Contractual Obligations

A substantial portion of the Company's core drill purchases are financed through capital leases. Payments for the fiscal year ending September 30, 2010 under these capital leases were \$485,473. The following fiscal year payments are due under these leases: \$319,482 (2011), \$143,939 (2012), \$140,683 (2013) and \$93,789 (2014).

Timberline Drilling also owns a fleet of vehicles, trucks and fork-lifts, as well as land and a building, for its drilling operations. Other equipment, vehicles and property were financed with notes collateralized by the equipment, vehicles or property. Payments for the fiscal year ending September 30, 2010 under these notes were \$363,145. The following fiscal year payments are due under these financing arrangements: \$508,907 (2011), \$322,965 (2012), \$315,290 (2013), and \$98,668 (2014).

Timberline and its subsidiaries lease office space and storage facilities. All of these facilities, which we believe are adequate for our needs for the foreseeable future, are leased. Under the current leases, we paid rental payments of \$205,116 in the fiscal year ending September 30, 2010. The current leases call for the following fiscal year payments: \$174,973 (2011), \$101,220 (2012), and \$34,305 (2013).

For additional information, please refer to Notes 9 and 10 of the consolidated financial statements of the Company, contained in Item 8 of this Annual Report.

Certain information contained in this "Management Discussion and Analysis" constitutes forward looking information and actual results could differ from estimates, expectations or beliefs contained in such statements.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Not Applicable.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

**TIMBERLINE RESOURCES CORPORATION AND
SUBSIDIARIES**

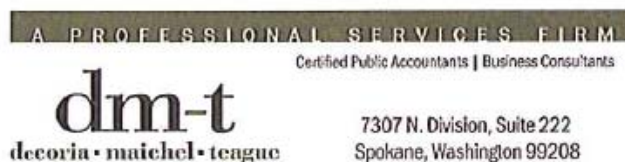
Consolidated Financial Statements

September 30, 2010 and 2009

Timberline Resources Corporation and Subsidiaries

Contents

	<u>Page</u>
<i>FINANCIAL STATEMENTS:</i>	
<i>Report of Registered Public Accounting Firm</i>	38
<i>Consolidated balance sheets</i>	39
<i>Consolidated statements of operations and comprehensive income (loss)</i>	40
<i>Consolidated statements of changes in stockholders' equity</i>	41-42
<i>Consolidated statements of cash flows</i>	43-44
<i>Notes to consolidated financial statements</i>	45-64



REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders of Timberline Resources Corporation:

We have audited the accompanying consolidated balance sheets of Timberline Resources Corporation ("the Company") as of September 30, 2010 and 2009, and the related consolidated statements of operations and comprehensive income (loss), changes in stockholders' equity and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Timberline Resources Corporation as of September 30, 2010 and 2009, and the results of its consolidated operations and cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

DeCoria, Maichel & Teague P.S.

DeCoria, Maichel & Teague, P.S.

Spokane, Washington
December 16, 2010

[TABLE OF CONTENTS](#)

**TIMBERLINE RESOURCES CORPORATION AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS**

	September 30, 2010	September 30, 2009
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	\$ 4,638,674	\$ 969,784
Accounts receivable, net of allowance for doubtful accounts of none and \$257,456, respectively	908,358	1,422,951
Materials and supplies inventory	1,238,369	1,088,428
Assets held for sale	319,291	-
Prepaid expenses and other current assets	394,557	609,545
Current portion of deferred financing cost with related party, net	27,273	-
TOTAL CURRENT ASSETS	7,526,522	4,090,708
PROPERTY, MINERAL RIGHTS AND EQUIPMENT:		
Mineral rights	12,162,342	47,000
Property and equipment, net	7,099,168	6,255,531
TOTAL PROPERTY, MINERAL RIGHTS AND EQUIPMENT	19,261,510	6,302,531
OTHER ASSETS:		
Investment in joint venture	621,000	621,000
Restricted cash	379,952	42,687
Deposits and other assets	148,512	108,777
Deferred financing cost with related party, net of current portion	15,909	-
Available-for-sale equity security (cost-\$50,000)	506,600	50,000
Goodwill	2,808,524	2,808,524
TOTAL OTHER ASSETS	4,480,497	3,630,988
TOTAL ASSETS	\$ 31,268,529	\$ 14,024,227
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Accounts payable	\$ 2,505,617	\$ 1,222,901
Accrued expenses	550,565	813,418
Accrued payroll and benefits	608,386	247,932
Accrued taxes	65,720	473,865
Current portion of long term debt	444,884	159,320
Current portion of obligations under capital leases	287,946	403,820
Current portion of customer advances	150,000	600,000
Accrued interest on convertible note payable to related party	41,667	-
Deferred revenue	45,000	-
TOTAL CURRENT LIABILITIES	4,699,785	3,921,256
LONG-TERM LIABILITIES:		
Convertible note payable to related party	5,000,000	5,000,000
Long term debt, net of current portion	680,969	237,638
Obligations under capital leases, net of current portion	341,316	167,632
Asset retirement obligation	259,467	-
Deferred income taxes	852,122	-
Customer advances, net of current portion	-	150,000
Accrued interest on convertible note payable to related party	-	477,916
TOTAL LONG-TERM LIABILITIES	7,133,874	6,033,186
COMMITMENTS AND CONTINGENCIES (NOTE 18)	-	-
STOCKHOLDERS' EQUITY:		
Preferred stock, \$0.01 par value; 10,000,000 shares authorized, none issued and outstanding	-	-
Common stock, \$0.001 par value; 100,000,000 shares authorized, 55,649,064 and 36,045,111 shares issued and outstanding, respectively	55,649	36,045
Additional paid-in capital	49,803,825	29,164,116
Accumulated deficit	(30,881,204)	(25,130,376)
Accumulated other comprehensive income:		
Unrealized gain on available-for-sale equity security	456,600	-
TOTAL STOCKHOLDERS' EQUITY	19,434,870	4,069,785
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 31,268,529	\$ 14,024,227

See accompanying notes to consolidated financial statements.

TIMBERLINE RESOURCES CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (LOSS)

	Year Ended September 30,	
	2010	2009
REVENUES	\$ 20,733,337	\$ 13,242,093
COST OF REVENUES	16,361,527	12,149,518
GROSS PROFIT	4,371,810	1,092,575
OPERATING EXPENSES:		
Mineral exploration expenses	2,221,262	493,389
Salaries and benefits	2,123,787	2,906,938
Insurance expense	491,175	513,642
Professional fees expense	947,550	1,274,895
Severance benefits (recovery)	51,300	(350,000)
Loss on sale of equipment	214,838	22,524
Other general and administrative expenses	2,383,284	1,930,704
TOTAL OPERATING EXPENSES	8,433,196	6,792,092
LOSS FROM OPERATIONS	(4,061,386)	(5,699,517)
OTHER INCOME (EXPENSE):		
Other income	188,080	27,798
Foreign exchange loss	(4,073)	-
Loss on derivative	-	(154,064)
Related party interest income	2,467	-
Interest income	14,386	15,314
Related party interest expense	(556,625)	(477,916)
Interest expense	(124,056)	(841,111)
TOTAL OTHER EXPENSE	(479,821)	(1,429,979)
NET LOSS BEFORE INCOME TAXES	(4,541,207)	(7,129,496)
INCOME TAX BENEFIT	408,031	-
NET LOSS FROM CONTINUING OPERATIONS	(4,133,176)	(7,129,496)
LOSS FROM DISCONTINUED OPERATIONS, NET OF TAX	(1,617,652)	(179,132)
NET LOSS	\$ (5,750,828)	\$ (7,308,628)
OTHER COMPREHENSIVE INCOME:		
Unrealized gain on available-for-sale equity security	456,600	-
COMPREHENSIVE LOSS	\$ (5,294,228)	\$ (7,308,628)
NET LOSS PER SHARE AVAILABLE TO COMMON STOCKHOLDERS		
BASIC AND DILUTED:		
CONTINUING OPERATIONS	\$ (0.09)	\$ (0.21)
DISCONTINUED OPERATIONS	(0.04)	(0.01)
NET LOSS	\$ (0.13)	\$ (0.22)
WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING, BASIC AND DILUTED	45,153,565	33,698,856

See accompanying notes to consolidated financial statements.

TIMBERLINE RESOURCES CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
FOR THE YEARS ENDED SEPTEMBER 30, 2010 AND 2009

	Common Stock		Additional	Accumulated	Accumulated	Total
	Shares	Amount	Paid-in	Deficit	Other Comprehensive Income	Stockholders' Equity
Balance, September 30, 2008	28,739,903	\$ 28,739	\$ 21,343,416	\$ (17,821,748)	\$ -	\$ 3,550,407
Common stock issued for options exercised	35,000	35	(35)	-	-	-
Common stock issued for conversion of short term convertible note	5,555,556	5,556	4,994,444	-	-	5,000,000
Common stock bonuses to employees	129,000	129	81,681	-	-	81,810
Common stock bonuses to directors	100,000	100	78,900	-	-	79,000
Common stock issued for put option exercised	535,652	536	245,864	-	-	246,400
Common stock issued for settlement of accrued offering and acquisition costs	950,000	950	345,800	-	-	346,750
Vested portion of stock options granted	-	-	2,074,046	-	-	2,074,046
Net loss	-	-	-	(7,308,628)	-	(7,308,628)
Balance, September 30, 2009	<u>36,045,111</u>	<u>\$ 36,045</u>	<u>\$ 29,164,116</u>	<u>\$ (25,130,376)</u>	<u>\$ -</u>	<u>\$ 4,069,785</u>

See accompanying notes to consolidated financial statements.

TIMBERLINE RESOURCES CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
FOR THE YEARS ENDED SEPTEMBER 30, 2010 AND 2009

	Common Stock		Additional	Accumulated	Accumulated	Total
	Shares	Amount	Paid-in	Deficit	Other Comprehensive Income	Stockholders' Equity
Balance, September 30, 2009	36,045,111	\$ 36,045	\$ 29,164,116	\$ (25,130,376)	\$ -	\$ 4,069,785
Common stock, warrants and options issued for acquisition	14,301,380	14,301	15,383,862	-	-	15,398,164
Common stock and warrants issued for cash at \$1.00 per unit, net of offering costs	3,003,400	3,003	2,674,642	-	-	2,677,645
Warrants issued in connection with private placement	-	-	129,517	-	-	129,517
Common stock issued for warrants exercised	1,085,944	1,086	541,886	-	-	542,972
Common stock issued for options exercised	1,176,729	1,176	441,765	-	-	442,941
Common stock bonuses to employees	36,500	37	41,938	-	-	41,975
Vested portion of stock options granted	-	-	1,426,099	-	-	1,426,099
Unrealized gain on available-for-sale equity security	-	-	-	-	456,600	456,600
Net loss	-	-	-	(5,750,828)	-	(5,750,828)
Balance, September 30, 2010	<u>55,649,064</u>	<u>\$ 55,649</u>	<u>\$ 49,803,825</u>	<u>\$ (30,881,204)</u>	<u>\$ 456,600</u>	<u>\$ 19,434,870</u>

See accompanying notes to consolidated financial statements.

TIMBERLINE RESOURCES CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year Ended September 30,	
	2010	2009
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	\$ (5,750,828)	\$ (7,308,628)
Adjustments to reconcile net loss to net cash used by operating activities:		
Depreciation and amortization	1,504,057	1,367,192
Loss on disposal of equipment	215,873	108,283
Stock based compensation	1,468,074	2,234,856
Impairment of mineral rights	35,000	90,000
Impairment of property and equipment	132,993	-
Accretion of asset retirement obligation	9,378	-
Other non cash compensation	33,845	-
Inventory write-down	289,942	-
Amortization of deferred financing cost with related party	6,818	-
Deferred income taxes	(408,031)	-
Amortization of deferred financing cost	-	202,550
Deferred offering and acquisition costs	-	923,957
Allowance for doubtful accounts	-	106,716
Loss on derivative	-	154,064
Severance recovery	-	(350,000)
Accrued offering and acquisition costs	-	(577,207)
Changes in assets and liabilities:		
Accounts receivable	514,593	1,865,484
Materials and supplies inventory	(439,883)	956,795
Assets held for sale	(228,641)	-
Prepaid expenses and other current assets, deposits and other assets	144,937	(26,623)
Accounts payable	1,282,716	(936,956)
Accrued expenses	(262,853)	(132,391)
Accrued payroll and other benefits	360,454	(234,782)
Accrued taxes	(408,145)	(1,699,497)
Deferred revenue	45,000	(27,315)
Accrued interest on convertible note payable to related party, due at maturity	(436,249)	477,916
Accrued severance	-	(50,000)
Net cash used by operating activities	(1,890,950)	(2,855,586)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of property, mineral rights and equipment	(1,092,856)	(312,877)
Change in restricted cash	(283,007)	243,723
Proceeds from sale of equipment	26,805	1,141,046
Net cash acquired in acquisition of Staccato Gold Resources Ltd.	4,421,033	-
Note receivable from related party	(100,000)	-
Repayment of note receivable from related party	100,000	-
Net cash provided by investing activities	3,071,975	1,071,892
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from issuances of stock and warrants, net of stock offering costs	2,807,162	-
Proceeds from exercise of warrants	542,972	-
Proceeds from exercise of options	442,941	-
Payments on long term debt	(223,441)	(341,411)
Deferred financing costs paid to related party	(50,000)	-
Payments on capital leases	(431,769)	(542,614)
Payments on customer advances	(600,000)	(250,000)
Repayment of bridge loan financing	-	(8,000,000)
Proceeds from convertible note payable to related party	-	5,000,000
Proceeds from short term convertible note	-	5,000,000
Proceeds from customer advances	-	1,000,000
Proceeds from long term debt	-	150,000
Net cash provided by financing activities	2,487,865	2,015,975

See accompanying notes to consolidated financial statements.

TIMBERLINE RESOURCES CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year Ended September 30,	
	2010	2009
Net increase in cash and cash equivalents	3,668,890	232,381
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	<u>969,784</u>	<u>737,503</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u><u>\$ 4,638,674</u></u>	<u><u>\$ 969,784</u></u>

SUPPLEMENTAL CASH FLOW DISCLOSURES

Interest paid in cash	\$ 1,577,292	\$ 237,718
Income taxes paid in cash	-	750,123

NON-CASH FINANCING AND INVESTING ACTIVITIES

Fair value of common stock, warrants and options issued in connection with an acquisition (see Note 7)	\$ 15,398,164	\$ -
Initial measurement of asset retirement obligation	250,089	-
Long term debt issued for property and equipment purchase	952,336	-
Capital lease for equipment purchase	489,579	88,405
Other current assets exchanged for equipment	100,000	104,220
Equipment loan paid with new note	128,263	180,692
Warrants issued to brokers acting as agents for a private placement	129,517	-
Conversion of short term convertible note into common stock	-	5,000,000
Transfer of land to joint venture	-	621,000
Settlement of accrued offering and acquisition costs with common stock	-	346,750
Settlement of put option with common stock	-	246,400
Equipment exchanged for other current assets	-	100,000

See accompanying notes to consolidated financial statements.

TIMBERLINE RESOURCES CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2010

NOTE 1 – ORGANIZATION AND DESCRIPTION OF BUSINESS:

Timberline Resources Corporation (“Timberline” or “the Company”) was incorporated in August of 1968 under the laws of the State of Idaho as Silver Crystal Mines, Inc., for the purpose of exploring for precious metal deposits and advancing them to production.

In 2006, the Company acquired Kettle Drilling, Inc. (“Kettle”) and its Mexican subsidiary, World Wide Exploration S.A. de C.V. (“World Wide”). Kettle provides drilling services to the mining and mineral exploration industries across North America and worldwide. In September 2008, Kettle Drilling, Inc. changed its name to Timberline Drilling Incorporated (“Timberline Drilling”).

On June 2, 2010, the Company acquired Staccato Gold Resources Ltd. (“Staccato”), a Canadian corporation, engaged in the exploration for precious metal deposits and advancing them to production (See Note 7).

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

- a. *Basis of Presentation* – This summary of significant accounting policies is presented to assist in understanding the financial statements. The financial statements and notes are representations of the Company’s management, which is responsible for their integrity and objectivity. These accounting policies conform to accounting principles generally accepted in the United States of America and have been consistently applied in the preparation of the financial statements.
- b. *Principles of Consolidation* – The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries after elimination of the intercompany accounts and transactions.
- c. *Exploration Expenditures* – All exploration expenditures are expensed as incurred. Significant property acquisition payments for active exploration properties are capitalized. If no mineable ore body is discovered, previously capitalized costs are expensed in the period the property is abandoned.
- d. *Fair Value of Financial Instruments* – The Company’s financial instruments include cash, restricted cash, accounts receivable, investments, accounts payable, derivatives and accrued expenses, and are carried at fair value. The carrying value of restricted cash, notes payable, capital leases, customer advances, and convertible note payable to related party approximate fair value based on the contractual terms of those instruments.
- e. *Cash Equivalents* – For the purposes of the statement of cash flows, the Company considers all highly liquid investments with original maturities of three months or less to be cash equivalents. Balances are insured by the Federal Deposit Insurance Corporation up to \$250,000 at each financial institution.
- f. *Restricted Cash* – Restricted cash represents investments in money market funds and are restricted as collateral for bonds held for exploration permits.
- g. *Estimates and Assumptions* – The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities at the dates of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Significant areas requiring the use of management assumptions and estimates relate to asset impairments, inventory net realizable value and asset retirement obligations. Actual results could differ from these estimates and assumptions and could have a material effect on the Company’s reported financial position and results of operations.

TIMBERLINE RESOURCES CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2010

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, (continued):

- h. *Investments* – Available-for-sale securities are initially recorded at cost and then carried at fair value, with unrealized gains or losses recorded as a component of equity, unless a decline in value of the security is considered other than temporary. Realized gains and losses and other than temporary impairments are recorded in the statement of operations. The Company also has a 50% interest in a joint venture at its Butte Highlands Gold Project (see Note 5). Given that the Company's 50% interest in the joint venture is carried to production, the Company does not have management control over operating decisions of the joint venture until its joint venture partner's investment in the project, less \$2 million, is recovered by the joint venture partner out of future production; and the Company has no risk of loss from expenses incurred by the joint venture until production, the Company is carrying its investment in the joint venture at cost on its consolidated balance sheet.
- i. *Revenue Recognition* – The Company recognizes drilling service revenues as the drilling services are provided to the customer based on the actual amount drilled for each contract on a per foot or per hour drilled basis. In some cases, the customer is responsible for mobilization and stand-by costs. Mobilization is charged to a customer when the Company deploys its personnel and equipment to a specific drilling site. Stand-by is charged to a customer when the Company deploys its personnel and equipment to a specific drilling site but, for reasons beyond the Company's control, drilling activities are not able to take place. Revenue related to reimbursement of mobilization and stand-by costs is recognized in the same period as the costs are incurred by the Company. The specific terms of each drilling job are agreed to by the customer and the Company prior to the commencement of drilling. Contract losses are not recognized as the Company's agreements with its customers do not put the Company at a risk of loss.
- j. *Accounts Receivable* – Accounts receivable are carried at original invoice amount less an estimate for doubtful accounts. Management determines the allowance for doubtful accounts by regularly evaluating individual customer receivables and considering a customer's financial condition, credit history, and current economic conditions. Trade receivables are written off when deemed uncollectible. Recoveries of receivables previously written off are recorded as income when received.
- k. *Materials and Supplies Inventory* – Inventories consist primarily of parts, operating supplies, drill rods and drill bits. The Company values its materials and supplies inventory, with the exception of drill rods, at the lower of average cost or market. Drill rods are valued using their average cost less an allowance for rod usage on a per foot drilled basis. Allowances are recorded for inventory considered to be in excess or obsolete.
- l. *Property and Equipment* – Property and equipment are stated at cost. Depreciation of property and equipment is calculated using the straight-line method over the estimated useful lives of the assets, which ranges from three to fifteen years. Maintenance and repairs are charged to operations as incurred. Significant improvements are capitalized and depreciated over the useful life of the assets. Gains or losses on disposition or retirement of property and equipment are recognized in operating expenses.
- m. *Assets Held under Capital Leases* – Assets held under capital leases are recorded at the lower of the net present value of the minimum lease payments or the fair value of the leased assets at the inception of the lease. Amortization expense is computed using the straight-line method over the shorter of the estimated useful lives of the assets or the period of the related lease.
- n. *Review of Carrying Value of Property, Mineral Rights and Equipment for Impairment* – The Company reviews the carrying value of property, mineral rights and equipment for impairment whenever events and circumstances indicate that the carrying value of an asset may not be recoverable from the estimated future cash flows expected to result from its use and eventual disposition. In cases where undiscounted expected future cash flows are less than the carrying value, an impairment loss is recognized equal to an amount by which the carrying value exceeds the fair value of assets. The factors considered by management in performing this assessment include current operating results, trends and prospects, the manner in which the property is used, the effects of obsolescence, demand, competition, and other economic factors. Based on this assessment, it was determined that our East Camp Douglas property was fully impaired at September 30, 2010 and the remaining \$35,000 in carrying value was written off to mineral exploration expenses during the year ended September 30, 2010. No other properties were determined to be impaired at September 30, 2010. At September 30, 2009, it

TIMBERLINE RESOURCES CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2010

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, (continued):

was determined that our East Camp Douglas, Gold Gate and Long Canyon properties were impaired and \$90,000 in carrying values were written off to mineral exploration expenses during the year ended September 30, 2009.

- o. *Asset Retirement Obligations* – A liability is recognized for the present value of estimated environmental remediation (asset retirement obligation), in the period in which the liability is incurred if a reasonable estimate of fair value can be made. The offsetting balance is charged to the related long-lived asset. Adjustments are made to the liability for changes resulting from passage of time and changes to either the timing or amount of the original present value estimate underlying the obligation. The Company has an asset retirement obligation associated with its joint venture at the Butte Highlands Gold Project (See Note 12).
- p. *Provision for Income Taxes* – Income taxes are provided based upon the liability method of accounting. Under this approach, deferred income taxes are recorded to reflect the tax consequences in future years of differences between the tax basis of assets and liabilities and their financial reporting amounts at each year-end. A valuation allowance is recorded against the deferred tax asset if management believes it is more likely than not that some portion or all of the deferred tax assets will not be realized (See Note 13).
- q. *Translation of Foreign Currencies* – All amounts are presented in US dollars. The Company’s discontinued operations in Mexico are translated at average rates of exchange for the year. The assets and liabilities of the Mexican operation are translated at the exchange rate in effect at the balance sheet date. Foreign translation and transaction gains (losses) of \$142,654 and \$(74,779) for the years ended September 30, 2010 and 2009, respectively, have been included in the current period net loss as a component of loss from discontinued operations. The Company also has a Canadian subsidiary that was acquired in June 2010 (See Note 7). The operations of the Canadian subsidiary are translated at average rates of exchange for the year. The assets and liabilities of the Canadian subsidiary are translated at the exchange rate in effect at the balance sheet date. Foreign translation and transaction losses from continuing operations of \$4,073 and none for the years ended September 30, 2010 and 2009, respectively, have been included in the current period net loss as a component of other expense.
- r. *Stock-based Compensation* – The Company estimates the fair value of its stock based compensation using the Black-Scholes model, which requires the input of some subjective assumptions. These assumptions include estimating the length of time employees will retain their vested stock options before exercising them (“expected life”), the estimated volatility of the Company’s common stock price over the expected term (“volatility”), employee forfeiture rate, the risk-free interest rate and the dividend yield. Changes in the subjective assumptions can materially affect the estimate of fair value of stock-based compensation.
- s. *Goodwill* – Goodwill relates to the acquisition of Timberline Drilling. At least annually, goodwill is tested for impairment by applying a fair value based test. In assessing the value of goodwill, assets and liabilities are assigned to the reporting units and a discounted expected cash flow analysis is used to determine fair value. There was no impairment loss revealed by this test as of September 30, 2010 or 2009.
- t. *Net Loss per Share* – Basic EPS is computed as net income (loss) available to common shareholders divided by the weighted average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur from common shares issuable through stock options, warrants, and other convertible securities.

The dilutive effect of convertible and outstanding securities as of September 30, 2010 and 2009 is as follows:

	2010	2009
Stock options	6,203,641	6,235,168
Warrants	8,050,375	1,337,934
Convertible debt	3,333,333	3,651,944
Total possible dilution	<u>17,587,349</u>	<u>11,225,046</u>

TIMBERLINE RESOURCES CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2010

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, (continued):

At September 30, 2010 and 2009, the effect of the Company's outstanding options and common stock equivalents would have been anti-dilutive. Accordingly, only basic EPS is presented.

- u. *Derivative Instruments* –The Company follows established accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities. Those standards require that an entity recognize all derivatives as either assets or liabilities in the balance sheet and measure those instruments at fair value. The Company does not use derivative instruments to hedge exposures to cash flow, market or foreign currency risks. For a derivative not designated as a hedging instrument, the gain or loss is recognized in the statement of operations in the period of change.
- v. *New Accounting Pronouncements* – In September 2006, the Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") was updated to establish a framework for measuring fair value and expand disclosure about fair value measurements, but does not require any new fair value measurements. Effective October 1, 2008, the Company adopted the updated guidance for our financial assets and financial liabilities without a material effect on the Company's consolidated financial statements. In February 2008, the FASB issued an update to the guidance which delayed the effective date for non-financial assets and non-financial liabilities to fiscal years beginning after November 15, 2008. Effective October 1, 2009, the Company adopted the updated guidance for non-financial assets and non-financial liabilities without a material effect on the Company's consolidated financial statements.

In December 2007, the ASC guidance for business combinations was updated to provide new guidance for recognizing and measuring identifiable assets and goodwill acquired, liabilities assumed, and any noncontrolling interest in the acquisition. The updated guidance also provides disclosure requirements to enable users of the financial statements to evaluate the nature and financial effects of the business combination. Effective October 1, 2009, the Company adopted the updated guidance for business combinations.

In December 2007, the ASC guidance for non-controlling interests was updated to establish accounting and reporting standards for minority interests, which will be re-characterized as non-controlling interests and classified as a component of equity. The updated guidance requires retroactive adoption of the presentation and disclosure requirements for existing minority interests. The updated guidance is effective for fiscal years beginning on or after December 15, 2008 and interim periods within those fiscal years. Effective October 1, 2009 the Company adopted the updated guidance without a material effect on the Company's consolidated financial statements.

In March 2008, the ASC guidance for derivatives and hedging was updated to require enhanced disclosures about an entity's derivative and hedging activities and thereby improve the transparency of financial reporting. The updated guidance is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008, with early application encouraged. The updated guidance encourages, but does not require, comparative disclosures for earlier periods at initial adoption. Effective October 1, 2009 the Company adopted the updated guidance without a material effect on the Company's consolidated financial statements.

In May 2008, the ASC guidance identifying the sources of accounting principles and the framework for selecting the principles to be used in the preparation of financial statements of nongovernmental entities that are presented in conformity with generally accepted accounting principles in the United States was updated. The guidance was effective November 15, 2008 and its adoption did not have a material effect on the Company's consolidated financial statements.

In May 2009, the ASC guidance for subsequent events was updated to establish general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued. This statement is effective for interim and annual periods ending after June 15, 2009. Accordingly, the Company adopted the updated guidance in its quarter ending June 30, 2009. The adoption of this statement did not have a material effect on the Company's consolidated financial statements.

TIMBERLINE RESOURCES CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2010

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, (continued):

In June 2009, the ASC guidance for consolidation accounting was updated to require an analysis to determine whether a variable interest gives the entity a controlling financial interest in a variable interest entity. This statement requires an ongoing reassessment and eliminates the quantitative approach previously required for determining whether an entity is the primary beneficiary. This statement is effective for fiscal years beginning after Nov. 15, 2009. Accordingly, the Company will adopt this updated guidance in fiscal year 2011 and is currently evaluating the impact of adopting this guidance on the consolidated financial statements.

In January 2010, the ASC guidance for fair value measurements was updated to require additional disclosures related to movements of assets among Levels 1 and 2 of the three-tier fair value hierarchy. Also, a reconciliation of purchases, sales, issuance, and settlements of anything valued with a Level 3 method is required. Disclosure regarding fair value measurements for each class of assets and liabilities will be required. The updated guidance was adopted by the Company in its quarter ending December 31, 2009, except for disclosures about the activity in Level 3 fair value measurements which are effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years. Adoption of this updated guidance did not have a material impact on the Company's consolidated financial statements.

- w. *Reclassifications* – Certain reclassifications have been made to the 2009 financial statements in order to conform to the 2010 presentation. These reclassifications have no effect on net loss, total assets or accumulated deficit as previously reported.

NOTE 3 – FAIR VALUE OF FINANCIAL INSTRUMENTS:

Effective October 1, 2008 for financial assets and liabilities, and October 1, 2009 for non-financial assets and liabilities, the Company has adopted expanded disclosure requirements to include the following information for each major category of assets and liabilities that are measured at fair value on a recurring or non recurring basis:

- a. the fair value measurement;
- b. the level within the fair value hierarchy in which the fair value measurements in their entirety fall, segregating fair value measurements using quoted prices in active markets for identical assets or liabilities (Level 1), significant other observable inputs (Level 2), and significant unobservable inputs (Level 3);
- c. for fair value measurements using significant unobservable inputs (Level 3), a reconciliation of the beginning and ending balances, separately presenting changes during the period attributable to the following:
 - 1) total gains or losses for the period (realized and unrealized), segregating those gains or losses included in earnings (or changes in net assets), and a description of where those gains or losses included in earnings (or changes in net assets) are reported in the statement of income (or activities);
 - 2) the amount of these gains or losses attributable to the change in unrealized gains or losses relating to those assets liabilities still held at the reporting period date and a description of where those unrealized gains or losses are reported;
 - 3) purchases, sales, issuances, and settlements (net); and
 - 4) transfers in and/or out of Level 3.

TIMBERLINE RESOURCES CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2010

NOTE 3 – FAIR VALUE OF FINANCIAL INSTRUMENTS, (continued):

The table below sets forth our financial assets and liabilities that were accounted for at fair value on a recurring basis as of September 30, 2010 and 2009, respectively, and the fair value calculation input hierarchy level that we have determined applies to each asset and liability category.

		<u>2010</u>	<u>2009</u>	<u>Input Hierarchy Level</u>
Assets:				
Cash and cash equivalents	\$	4,638,674	\$ 969,784	Level 1
Restricted cash		379,952	42,687	Level 1
Available-for-sale equity security		506,600	50,000	Level 2

NOTE 4 – PROPERTY, MINERAL RIGHTS AND EQUIPMENT:

The following is a summary of property, mineral rights and equipment and accumulated depreciation at September 30, 2010 and 2009:

	<u>Expected Useful Lives (years)</u>	<u>2010</u>	<u>2009</u>
Equipment and vehicles	5-10	\$ 10,307,144	\$ 9,312,806
Office equipment and furniture	3-10	236,688	261,664
Land	-	114,188	51,477
Mineral rights	-	12,162,342	47,000
Asset retirement cost	-	250,089	-
Building and leasehold improvements	5-15	349,813	149,377
Total property, mineral rights and equipment		23,420,264	9,822,324
Less accumulated depreciation		(4,158,754)	(3,519,793)
Property, mineral rights and equipment, net		\$ 19,261,510	\$ 6,302,531

Property and equipment includes assets (primarily core drills and related equipment) held under capital leases of \$1,612,443 and \$1,592,273 at September 30, 2010 and 2009. Related amortization of assets held under capital leases included in accumulated depreciation was \$422,813 and \$509,920 at September 30, 2010 and 2009, respectively (See Note 9).

Depreciation expense for the years ended September 30, 2010 and 2009 was \$1,504,057 and \$1,367,192, respectively.

During the years ended September 30, 2010 and 2009, respectively, the Company acquired \$100,000 and \$104,220 in equipment and vehicles in exchange for other current assets.

During the year ended September 30, 2009, the Company transferred its Butte Highlands land, valued at \$621,000 to the Butte Highlands Joint Venture, LLC (“BHJV”) in return for a 50% carried interest in BHJV (See Note 5).

NOTE 5 – INVESTMENT IN JOINT VENTURE:

In July 2009, the Company entered into a Joint Venture Operating Agreement with Highland Mining, LLC (“Highland”), an entity controlled by Ronald Guill, a director of the Company. The joint venture entity, Butte Highlands JV, LLC (“BHJV”) was created for the purpose of developing and mining the Butte Highlands Gold Project. As a result of its contribution of the Company’s 100% interest in the Butte Highlands Gold Project, carried on its balance sheet at the original purchase price of the Butte Highlands project (\$621,000) to BHJV, the Company

TIMBERLINE RESOURCES CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2010

NOTE 5 – INVESTMENT IN JOINT VENTURE, (continued):

holds a 50% interest in BHJV. Under terms of the agreement, the Company will be carried to production by Highland, which will fund all future project exploration and mine development costs.

Under the operating agreement for BHJV, Highland will contribute property and fund all future mine development costs at Butte Highlands. Both the Company's and Highlands's share of development costs will be paid from proceeds of future mine production. The BHJV operating agreement stipulates that Highland shall appoint a manager of BHJV and that Highland will manage BHJV until such time as all mine development costs, less \$2 million, are distributed to Highland out of the proceeds from future mine production.

NOTE 6 – AVAILABLE-FOR-SALE EQUITY SECURITY:

Available-for-sale equity security is comprised of 2,980,000 shares of common stock in Rae Wallace Mining Company ("RWMC"), which have been valued as described below. The following table summarizes the Company's available-for-sale equity security:

	Year Ended September 30,	
	2010	2009
Cost	\$ 50,000	\$ 50,000
Unrealized Gain	\$ 456,600	-
Fair Value	<u>\$ 506,600</u>	<u>\$ 50,000</u>

Management has determined the best measure of fair value to be the bid price of RWMC stock as quoted by the market maker in the stock as of September 30, 2010, which was \$0.17 per share. At September 30, 2009, the Company recorded its investment at its cost of \$50,000, which management believed approximated its fair value at that time.

RWMC is also a related party to the Company (See Note 11).

NOTE 7 – ACQUISITION OF STACCATO GOLD RESOURCES LTD.:

On June 2, 2010, the Company completed its acquisition of all of the issued and outstanding common shares of Staccato Gold Resources Ltd. ("Staccato"), by way of a court approved Plan of Arrangement under the Business Corporations Act (British Columbia) in accordance with the terms of an Arrangement Agreement, dated March 22, 2010, by and between the Company and Staccato. The acquisition was also approved by the Timberline stockholders and Staccato's securityholders. Staccato was a publicly held Canadian corporation engaged in the exploration of precious metals properties in Nevada. Timberline acquired Staccato in order to further the exploration and development of mineral properties owned or leased by Staccato, as well as to increase the working capital of the Company.

This transaction was accounted for as a business combination. The Company acquired all of the issued and outstanding common shares of Staccato in consideration for the issuance of one share of common stock of the Company for every seven common shares of Staccato and \$0.0001 in cash for each common share of Staccato. In addition, the Company acquired all of the issued and outstanding warrants to purchase common shares of Staccato and options to purchase common shares of Staccato, after giving effect to the exercise and cancellation of certain options immediately prior to closing, in consideration for the issuance by the Company of a warrant to purchase one share of common stock of the Company for every seven Staccato warrants or an option to purchase one share of common stock of the Company for every seven Staccato options, as applicable. Pre-acquisition Timberline shareholders own approximately 74% of the issued and outstanding common stock of the Company as of the acquisition date and former Staccato shareholders own approximately 26%. On a fully diluted basis, Timberline is owned 71% by pre-acquisition Timberline shareholders and 29% by former Staccato shareholders as of the acquisition date.

TIMBERLINE RESOURCES CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2010

NOTE 7 – ACQUISITION OF STACCATO GOLD RESOURCES LTD., (continued):

The purchase price of the transaction was \$15,435,199, consisting of the issuance of 14,301,380 shares of Timberline common stock valued at \$14,444,394; 6,352,437 warrants to purchase one share of Timberline common stock valued at \$889,341; 102,143 options to purchase one share of Timberline common stock valued at \$64,429; and cash of \$37,035. The Company incurred \$214,477 in expenses related to the acquisition, \$205,541 of which are included in professional fees expense, \$5,800 are included in mineral exploration expenses and \$3,136 are included in other general and administrative expenses in the consolidated statement of operations.

Timberline's common stock issued as consideration was valued based upon the closing price of \$1.01 per share of our common stock on the NYSE Amex on June 2, 2010. The warrants and options that were issued as consideration were valued on that date using the Black-Scholes pricing model, based upon the following principal assumptions:

	Warrants	Options
Risk-free interest rate	0.38%	0.22% - 1.30%
Dividend yield	N/A	N/A
Volatility factor	106.1%	57.7% - 121.6%
Remaining to expiry date – warrants (weighted average)	1.13 years	
Expected term - options		0.60 – 2.90 years

The purchase price allocation of the acquisition is summarized as follows:

Purchase price:	
Shares issued on acquisition	\$ 14,444,394
Warrants	889,341
Options	64,429
Cash	37,035
	<u>\$ 15,435,199</u>
Net assets acquired:	
Cash and cash equivalents	\$ 4,458,068
Other current assets	69,684
Restricted cash	54,258
Mineral rights and equipment, net	12,113,342
Deferred income taxes	(1,260,153)
	<u>\$ 15,435,199</u>

The consolidated statement of operations of the Company for the year ended September 30, 2010 includes expenses incurred by Staccato of \$1,277,744 and no revenue since the acquisition date.

The unaudited pro forma financial information below represents the combined results of the Company's operations as if the Staccato acquisition had occurred at the beginning of the periods presented. The unaudited pro forma financial information is presented for informational purposes only and is not indicative of the results of operations that would have occurred if the acquisition had taken place at the beginning of the periods presented, nor is it indicative of future operating results. The unaudited pro forma loss from operations, net loss and net loss per share available to common stockholders, basic and diluted, for the year ended September 30, 2010 includes non-recurring severance and professional expenses incurred by Staccato in the amount of \$1,622,248.

	Year ended September 30,	
	2010	2009
Revenues	\$ 20,733,337	\$ 13,242,093
Loss from operations	(6,748,356)	(8,225,189)
Net loss from continuing operations	(7,175,813)	(9,413,372)
Net loss per share from continuing operations available to common stockholders, basic and diluted	(0.13)	(0.20)

TIMBERLINE RESOURCES CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2010

NOTE 8 – CUSTOMER ADVANCES:

During the year ended September 30, 2009, Newmont USA Limited (“Newmont”) provided an advance payment for drilling services of \$1,000,000 to the Company and extended its contract with the Company through February 2011. The advance is to be repaid by twenty monthly payments of \$50,000 beginning May 15, 2009 and ending December 15, 2010. The advance was provided pursuant to a contract change order which did not contain any provisions for interest or prepayment penalties, nor any specified right of offset. As of September 30, 2010 and September 30, 2009, customer advances were \$150,000 and \$750,000, respectively. \$0 and \$150,000 of the remaining customer advance balance was classified as a long-term liability as of September 30, 2010 and 2009, respectively.

NOTE 9 – CAPITAL LEASES:

The Company finances a substantial portion of its core drilling equipment purchases through capital leases. Future minimum lease payments at September 30, 2010 for the related obligations under capital leases were:

Year Ending September 30,

2011	\$	319,482
2012		143,939
2013		140,683
2014		93,789
Total minimum lease payments		697,893
Less amount representing interest		(68,631)
Present value of minimum lease payments		629,262
Less obligations due within one year		(287,946)
Obligations under capital leases, due after one year	\$	341,316

NOTE 10 – LONG TERM DEBT:

Long term debt at September 30, 2010 and 2009 consists of the following:

	2010	2009
Notes payable to various lenders for vehicles and equipment, in monthly payments totaling \$26,098 per month, at rates ranging from 0.0% to 10.0% with a weighted average interest rate of approximately 6.5%. The notes are collateralized by vehicles, equipment, and accounts receivable.	\$ 1,125,853	\$ 396,958
Less current portion	(444,884)	(159,320)
	<u>\$ 680,969</u>	<u>\$ 237,638</u>
Debt outstanding will mature as follows:		
Year ending September 30,		
2011	\$ 444,884	
2012	286,308	
2013	297,849	
2014	96,812	
Total	<u>\$ 1,125,853</u>	

TIMBERLINE RESOURCES CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2010

NOTE 11 – RELATED PARTY TRANSACTIONS:

Information regarding related party notes payable is as follows at September 30, 2010 and 2009:

	<u>2010</u>	<u>2009</u>
Small Mine Development, LLC	\$ <u>5,000,000</u>	\$ <u>5,000,000</u>
Accrued interest on note payable to Small Mine Development, LLC	\$ <u>41,667</u>	\$ <u>477,916</u>
Related party interest expense	\$ <u>556,625</u>	\$ <u>477,916</u>

On October 31, 2008, the Company entered into a series of agreements in connection with a \$5 million loan from Small Mine Development, LLC (“SMD”). The loan documents included: a convertible note (the “Convertible Term Note”), a credit agreement (the “Credit Agreement”), a collateral assignment and pledge of stock and security agreement (the “Pledge Agreement”), a security agreement (the “Security Agreement”) and a right of first refusal over the Company’s Butte Highlands property (the “Right of First Refusal”).

The Convertible Term Note has a principal amount of \$5.0 million and is collateralized pursuant to the Security Agreement by a pledge of all of the stock of Timberline Drilling, Inc., pursuant to the Pledge Agreement, as well as a Deed of Trust covering the Company’s Butte Highlands property in Silver Bow county, Montana (the “Butte Highlands Property”).

Pursuant to the terms of the Credit Agreement, the Convertible Term Note bears interest at 10% annually, compounded monthly, with interest payments due at maturity on October 31, 2010. The Convertible Term Note, including accrued interest, is convertible into common stock by SMD at any time prior to payment of the note in full, at a conversion price of \$1.50 per share. Should the Company issue any form of equity security other than the Company’s common stock, SMD may also convert all or any portion of the outstanding amount under the Convertible Term Note into the new form of equity security at the issuance price of the new form of equity security. Management analyzed the conversion features contained in this note considering the guidance provided in the ASC for derivatives and hedging. Management’s conclusion was that these convertible features are conventional convertible instruments and thus would qualify for equity classification. As conventional convertible instruments, the embedded conversion options qualify for the scope exception provided in the guidance for derivatives and hedging, and therefore would not be bifurcated from the host instrument.

The Convertible Term Note was scheduled to be repaid on or before October 31, 2010, including interest due at maturity. In June 2010, SMD agreed to extend the Maturity Date of the Convertible Term Note to on or before April 30, 2012. All interest accrued through June 30, 2010 was paid by the Company to SMD at that time. The Company also paid a \$50,000 extension fee to SMD in consideration for the extension of the Convertible Term Note. The extension fee has been recorded as a deferred financing cost and is being amortized over the life of the loan. The Convertible Term Note was also amended to require interest accrued subsequent to June 30, 2010 to be paid by the Company to SMD monthly, rather than accruing interest to maturity. All other terms of the loan were unchanged. The Company has accounted for the extension of the Maturity Date as a loan modification.

The Convertible Term Note may be prepaid in whole or in part at any time without premium or penalty. If the Company defaults on the Convertible Term Note or any of the related agreements, SMD may declare the Convertible Term Note immediately due and payable, and the Company must pay SMD an origination fee in the amount of \$50,000.

Under the Right of First Refusal, the Company granted SMD a right of first refusal to purchase the Butte Highlands Property on the same terms as those of any bona fide offer from a third-party upon 60 days’ notice from the Company of any such offer. In addition, the Company granted SMD a right to develop the Butte Highlands Property on the same terms as those of any bona fide offer to develop the property from a third-party upon 60 days’ notice from the Company of any such offer.

TIMBERLINE RESOURCES CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2010

NOTE 11 – RELATED PARTY TRANSACTIONS, (continued):

Butte Highlands Joint Venture Agreement

On July 22, 2009, the Company entered into an Operating Agreement with Highland Mining, LLC (“Highland”), an affiliate of SMD, to form a 50/50 joint venture for development and mining of the Company’s Butte Highlands Gold Project. Under the terms of the operating agreement, the Company will contribute its Butte Highlands property to BHJV for a deemed value of \$2 million, and Highland will contribute property and fund all future mine development costs. Both the Company’s and Highland’s share of costs will be paid out of proceeds from future mine production.

Mr. Guill, a director of the Company and an owner of Highland, will be the manager of BHJV until such time as all mine development costs less \$2 million are distributed to Highland. At that time, a management committee will be formed with equal representation from Highland and the Company. Under the terms of the Operating Agreement, Highland will have preferential rights with respect to distributions until the investment by the Company is deemed equal to the investment by Highland.

During the years ended September 30, 2010 and 2009, Timberline Drilling, our wholly owned subsidiary, provided \$106,763 and \$431,184, respectively, in core drilling services to BHJV at the Butte Highlands Gold Project.

At September 30, 2010 and 2009, the Company has a receivable from BHJV for expenses incurred on behalf of BHJV in the amount of \$30,571 and \$167,073, respectively. This amount is included in prepaid expenses and other assets on the consolidated balance sheets at September 30, 2010 and 2009.

Swallow Consulting Agreement

In December 2009 the Company entered into an agreement with John Swallow, a former director and former executive of the Company, to provide advisory services as needed and requested by the Company through June 30, 2010. In exchange for these services the Company paid Mr. Swallow \$170,000.

Rae Wallace Mining Company

The Company is an affiliate of Rae Wallace Mining Company (“RWMC”), as it holds approximately 18% of the issued and outstanding stock of RWMC as of September 30, 2010.

In May 2010, the Company entered into an agreement with RWMC to provide bridge loan financing. An unsecured loan for \$100,000 was made by the Company to RWMC, with an annual interest rate of 12%, due August 31, 2010. In July 2010 the entire loan balance was repaid, along with \$2,467 of interest accrued up to the date of repayment, and the loan agreement was cancelled.

NOTE 12 – ASSET RETIREMENT OBLIGATION:

The Company has an asset retirement obligation (“ARO”) associated with the underground exploration program at the Butte Highlands Gold Project being performed by BHJV (see Note 5). The ARO resulted from the reclamation and remediation requirements of the Montana Department of Environmental Quality as outlined in the Company’s permit to carry out the exploration program.

Estimated reclamation costs were discounted using a credit adjusted risk-free interest rate of 5% from the time the Company expects to pay the retirement obligation to the time it incurred the obligation, which is estimated at 12 years.

TIMBERLINE RESOURCES CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2010

NOTE 12 – ASSET RETIREMENT OBLIGATION, (continued):

The following table summarizes activity in the Company's ARO.

	Year Ended
	September 30, 2010
Balance at September 30, 2009	\$ -
Initial measurement	250,089
Accretion expense	9,378
Balance at September 30, 2010	\$ 259,467

NOTE 13 – INCOME TAXES:

Significant components of income tax benefit for the years ended September 30, 2010 and 2009 are as follows:

	2010	2009
Current:		
Federal	\$ -	\$ -
State	-	-
Discontinued operations	-	145,089
Total current income tax benefit	-	145,089
Deferred:		
Federal	408,031	-
Foreign	-	-
Total deferred income tax provision	408,031	-
Total income tax benefit	\$ 408,031	\$ 145,089

The components of the Company's deferred taxes are as follows:

	2010	2009
Net deferred tax asset:		
Exploration costs	\$ 860,000	\$ 539,500
Property, mineral rights and equipment	(275,000)	(219,000)
Bad debt reserve	-	106,000
Intangible expenses	(167,000)	(72,000)
Foreign intangible expenses	(230,000)	-
Share based compensation	1,787,000	1,522,000
Foreign income tax credit carryforwards	443,000	442,800
Federal net operating losses	8,920,000	7,120,000
Foreign net operating losses	1,878,000	-
Total net deferred tax asset	13,216,000	9,439,300
Valuation allowance	(13,216,000)	(9,439,300)
Deferred tax asset	\$ -	\$ -

BH Minerals USA, Inc.

Net deferred tax liability:		
Property, mineral rights and equipment	(3,684,122)	-
Exploration costs	396,000	-
Federal net operating losses	2,436,000	-
Total deferred tax liability	(852,122)	-
Deferred tax liability	\$ 852,122	\$ -

TIMBERLINE RESOURCES CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2010

NOTE 13 – INCOME TAXES, (continued):

The federal income taxes of the Company's wholly owned subsidiary, BH Minerals USA, Inc., are not consolidated with those of the rest of the Company since BH Minerals USA, Inc. is wholly owned by the Company's Canadian subsidiary, Staccato Gold Resources Ltd.

As management of the Company cannot determine that it is more likely than not that the Company will realize the benefit of the net deferred tax asset, a valuation allowance equal to 100% of the net deferred tax asset has been recorded at September 30, 2010 and 2009.

Net loss before income taxes for the years ended September 30, 2010 and 2009 are as follows:

	<u>2010</u>	<u>2009</u>
Current:		
Domestic	\$ (4,494,555)	\$ (7,098,117)
Foreign	(1,664,304)	(355,600)
	<u>\$ (6,158,859)</u>	<u>\$ (7,453,717)</u>
	<u>2010</u>	<u>2009</u>
Statutory Federal income tax rate	34%	34%
Expected income tax benefit based on statutory rate	\$ (2,094,000)	\$ (2,534,300)
Permanent differences ⁽¹⁾	(116,031)	740,000
Effect of state taxes	(342,000)	(522,000)
Non-recognition due to increase in valuation allowance	2,144,000	2,316,300
Discontinued operations benefit	-	(145,089)
Total income tax benefit	<u>\$ (408,031)</u>	<u>\$ (145,089)</u>

⁽¹⁾ Includes tax loss carryforwards, foreign current income taxes, non-deductible insurance premiums, non-deductible meals and entertainment, and non-deductible penalties

The Company has concluded that the guidance regarding accounting for uncertainty in income taxes had no significant impact on our results of operations or financial position as of September 30, 2010 or 2009. Therefore, we do not have an accrual for uncertain tax positions as of September 30, 2010 or 2009. As a result, tabular reconciliation of beginning and ending balances would not be meaningful. If interest and penalties were to be assessed, we would charge interest to interest expense, and penalties to other operating expense. It is not anticipated that unrecognized tax benefits would significantly increase or decrease within 12 months of the reporting date.

At September 30, 2010, the Company has federal net operating loss carryforwards of approximately \$28,700,000 which will expire in fiscal years ending September 30, 2017 through September 30, 2030. \$21,617,000 of state net operating loss carryforwards will expire in fiscal years ending September 30, 2011 through September 30, 2030.

At September 30, 2010 the Company had \$443,000 of foreign tax credit carryforwards which expire in 2012 and 2013. The Company also has approximately \$6,000,000 in net operating loss carryforwards in Canada which will expire in fiscal years ending September 30, 2026 through September 30, 2030.

For the year ended September 30, 2010, the acquisition of Staccato Gold Resources Ltd. had a significant impact on our deferred tax position. The acquisition added a net deferred tax liability of \$852,122 related to the purchase accounting.

TIMBERLINE RESOURCES CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2010

NOTE 13 – INCOME TAXES, (continued):

The Tax Reform Act of 1986 substantially changed the rules relative to the use of net operating loss and general business credit carryforwards in the event of an “ownership change” of a corporation. Due to the change in ownership in 2004, the Company is restricted in the future use of net operating losses generated before the ownership change. As of September 30, 2010, this limitation is applicable to accumulated federal net operating losses of approximately \$2,040,000.

Certain estimates for income tax for the year ended September 30, 2009 used in calculating income tax for the year ended September 30, 2010 have been revised to reflect the actual amounts per the tax returns filed with federal and state tax authorities. These revisions had no effect on the current or prior year income tax provision (benefit), or deferred tax assets or liabilities.

NOTE 14 – COMMON STOCK, WARRANTS AND PREFERRED STOCK:

Private Placement

In November 2009, the Company initiated a private placement of the Company’s common stock. Under the private placement subscription agreement, the Company could sell up to 3,000,000 units at a price of \$1.00 per unit for a total of \$3,000,000. The Company reserved the right to increase the amount of the offering in the event that the offering was oversubscribed. Each unit consisted of one share of common stock and one half of one Class A Warrant; with each whole warrant exercisable to acquire one additional share of common stock at an exercise price of \$1.50 per share until May 31, 2010, and thereafter at an exercise price of \$1.75 per share until March 25, 2011. No registration rights were granted for the shares of common stock or the shares of common stock underlying the warrants. The units were sold for \$1.00 each, representing management’s estimate of the fair value of the unit. The Company sold a total of 3,003,400 units for gross proceeds of \$3,003,400 and the placement closed on November 23, 2009. The Company incurred \$196,238 in expenses with respect to the offering, resulting in net proceeds of \$2,807,162. In connection with the offering, the Company also issued 196,238 warrants, with the same terms of exercise as described above, to brokers acting as agents for the private placement valued at \$129,517. The value of the 1,697,938 issued warrants, using the Black-Scholes option pricing model with a risk free interest rate of 0.29%, stock price on the date of closing of \$1.18, volatility of 153.4%, dividend yield of 0% and an expected life equal to the term of the warrants, was \$1,120,441.

Warrant Repricing

In September 2009, the Company amended the terms of the Company’s outstanding warrants to encourage warrant holders to exercise their warrants. At September 30, 2009, the Company had 1,337,934 warrants outstanding with an exercise price of \$3.50 and expiration dates between September 30, 2009 and October 11, 2009. In order to induce the exercise of the warrants, the Company’s Board of Directors authorized that the exercise price of the warrants be reduced. The amended exercise price for each warrant was \$0.50. Additionally, to permit holders of the warrants adequate time to contemplate the repricing, the expiration dates of the warrants was extended until October 16, 2009. 1,085,944 of the 1,337,934 outstanding warrants were exercised by warrant holders on or before October 16, 2009, generating proceeds to the Company of \$542,972.

Acquisition of Staccato Gold Resources Ltd.

In June 2010, as part of the Company’s acquisition of Staccato, 6,352,437 warrants were issued in exchange for outstanding Staccato warrants at the June 2, 2010 acquisition date. The warrants have an exercise price of \$3.34 and have terms expiring between July 4, 2011 and August 16, 2011. The value of the 6,352,437 issued warrants, using the Black-Scholes option pricing model with a risk free interest rate of 0.38%, stock price on the date of closing the Staccato acquisition of \$1.01, volatility of 106.1%, dividend yield of 0% and an expected life equal to the term of the warrants, was \$889,341. This value was included as part of the cost of the acquisition (see Note 7).

TIMBERLINE RESOURCES CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2010

NOTE 14 – COMMON STOCK, WARRANTS AND PREFERRED STOCK, (continued):

Stock Issued on Conversion of Short Term Convertible Note

In October 2008, the Company entered into a short-term convertible note (the “Short-Term Convertible Note”) with Ronald and Stacey Guill in connection with a loan for \$5 million. The Short-Term Convertible Note principal automatically converted into 5,555,556 shares of Company stock (valued at \$0.90 per share) upon approval of the issuance of the additional shares for listing by the NYSE Amex. Regulatory approval was received in December 2008.

Stock Issued for Settlement of Put Option

In return for providing bridge loan financing to the Company during the year ended September 30, 2008, the lender received 160,000 shares of common stock of the Company. In addition, the lender received a put option for the 160,000 shares of common stock issued, exercisable ninety days from the maturity date of the bridge loan, to put some or all of the 160,000 common shares back to the Company at a redemption price of \$2.00 per share.

During the year ended September 30, 2009, the lender indicated its intention to exercise the put option and return the shares to the Company. The Company and the lender agreed that the Company would issue an additional 535,652 shares of common stock, valued at the trailing 30 day average closing price of the Company’s stock of \$0.46 per share, to the lender in lieu of settling the option with a cash payment. These shares were issued in March 2009 and a loss on the derivative of \$154,064 was recorded in the consolidated statement of operations for the year ending September 30, 2009.

Stock Issued for Settlement of Offering Costs Arising from the Proposed Acquisition of SMD

In October 2008, the Company and Ronald Guill mutually agreed by written consent to terminate the Stock Purchase Agreement previously entered into between the Company and Mr. Guill in February 2008, which would have provided for the purchase by the Company of all of Mr. Guill’s membership interests in SMD. The Company had engaged a full service investment banking and institutional securities firm to render an opinion to the Company’s Board as to whether the consideration to be paid by the Company for the membership interests of SMD was fair, from a financial point of view. The Company also engaged this firm to arrange for financing of the acquisition of SMD’s membership interests. All fees to be paid by the Company for these services were contemplated to be paid out of proceeds raised during the financing.

Subsequent to the termination of the acquisition of SMD and the failure of the investment banking firm to arrange financing, an invoice was received by the Company from the investment banking firm for the provision of the fairness opinion, as well as legal fees incurred by the firm during the course of the financing. The total amount charged for the services provided was \$923,957. In July 2009, the Company agreed to satisfy the outstanding invoice by payment of \$50,000 in cash and issuance of 950,000 common shares of the Company subject to approval by the NYSE Amex. The Stock Settlement and Release Agreement (the “Agreement”) between the Company and the investment banking firm was finalized in July 2009. As a result of the Agreement, the total expense incurred by the Company was \$396,750, comprised of the \$50,000 in cash and \$346,750, equal to the fair market value of the 950,000 shares of the Company as of the date of the Agreement. This expense has been included in professional fees in the consolidated statement of operations for the year ended September 30, 2009.

Stock Issued for Services

During the years ended September 30, 2010 and 2009, 36,500 and 229,000 shares of common stock, respectively, were issued to employees and directors of the Company as incentive bonuses under the Company’s 2005 Equity Incentive Plan (amended).

TIMBERLINE RESOURCES CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2010

NOTE 14 – COMMON STOCK, WARRANTS AND PREFERRED STOCK (continued):

Warrants

The following is a summary of the Company's warrants outstanding:

	Shares		Weighted Average Exercise Price
Outstanding at September 30, 2008	2,301,734	\$	2.45
Issued			
Exercised			
Expired	(963,800)		(1.00)
Outstanding at September 30, 2009	1,337,934		0.50 ⁽²⁾
Issued	1,697,938		1.75
Issued on acquisition of Staccato Gold Resources Ltd.	6,352,437		3.34
Exercised	(1,085,944)		0.50
Expired	(251,990)		(0.50)
Outstanding at September 30, 2010 ⁽¹⁾	8,050,375	\$	3.00

⁽¹⁾ These warrants expire as follows:

Warrants	Price	Expiration Date
1,697,938	\$1.75	March 25, 2011
2,485,488	\$3.34	July 4, 2011
1,744,500	\$3.34	July 18, 2011
1,362,857	\$3.34	August 9, 2011
759,592	\$3.34	August 16, 2011
<u>8,050,375</u>		

⁽²⁾ In September 2009, the Company amended the terms of its outstanding warrants to encourage holders to exercise their warrants. As a result, the exercise price of the warrants outstanding at September 30, 2009 was amended from \$3.50 per warrant to \$0.50, and the expiration date was extended from September 30, 2009 to October 16, 2009. 1,085,944 of these warrants were exercised during the year ended September 30, 2010 and the remaining 251,990 expired.

Preferred Stock

Timberline is authorized to issue up to 10,000,000 shares of preferred stock, \$.01 par value. The Board of Directors of Timberline is authorized to issue the preferred stock from time to time in series, and is further authorized to establish such series, to fix and determine the variations in the relative rights and preferences as between series, to fix voting rights, if any, for each series, and to allow for the conversion of preferred stock into Common Stock.

TIMBERLINE RESOURCES CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2010

NOTE 15 – STOCK OPTIONS:

The Company has established the 2005 Equity Incentive Plan (as amended by shareholders of the Company on May 28, 2010) to authorize the granting of up to 10,000,000 stock options to employees, directors and consultants. Upon exercise of options, shares are issued from the available authorized shares of the Company. Option awards are generally granted with an exercise price equal to the fair value of the Company's stock at the date of grant. The fair value of each option award was estimated on the date of grant using the assumptions noted in the following table.

	<u>2010</u>	<u>2009</u>
Expected volatility	57.7% - 129.7%	105.2% - 122.6%
Weighted-average volatility	126.5%	111.5%
Expected dividends	-	-
Expected term (in years)	0.6 - 3.0	2.0 - 3.0
Risk-free rate	0.22% - 1.38%	1.02% - 1.49%
Expected forfeiture rate	0% - 10%	10%

The following is a summary of the Company's options issued under the Stock Incentive Plan:

	<u>Shares</u>	<u>Weighted Average Exercise Price</u>
Outstanding at September 30, 2008	3,917,502	\$ 2.65
Granted	4,678,500	0.41
Exercised	(75,000)	(0.80)
Expired	(2,285,834)	(2.83)
Outstanding at September 30, 2009	<u>6,235,168</u>	<u>\$ 0.92</u>
Exercisable at September 30, 2009	<u>4,005,933</u>	<u>\$ 1.02</u>
Weighted average fair value of options granted during the year ended September 30, 2009		<u>\$ 0.31</u>
Outstanding at September 30, 2009	6,235,168	\$ 0.92
Granted ⁽¹⁾	1,587,143	0.89
Exercised	(1,277,003)	(0.44)
Expired and forfeited	(341,667)	(1.94)
Outstanding at September 30, 2010	<u>6,203,641</u>	<u>\$ 0.96</u>
Exercisable at September 30, 2010	<u>5,459,648</u>	<u>\$ 1.04</u>
Weighted average fair value of options granted during the year ended September 30, 2010		<u>\$ 0.56</u>

⁽¹⁾ Includes 102,143 options issued to holders of Staccato Gold Resources stock options pursuant to the agreement for the acquisition of Staccato Gold Resources Ltd by the Company.

TIMBERLINE RESOURCES CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2010

NOTE 15 – STOCK OPTIONS, (continued):

The average remaining contractual term of the options outstanding and exercisable at September 30, 2010 was 3.42 and 3.45 years, respectively. The average remaining contractual term of the options outstanding and exercisable at September 30, 2009 was 3.97 and 3.89 years, respectively. Of the options exercised, 301,668 were on a cashless basis resulting in the issuance of 201,394 shares based on the current price of the Company's stock on the date of exercise. The Company received \$442,941 from the exercise of the remaining 975,335 options. Options exercised during the year ending September 30, 2009 were exercised on a cashless basis, resulting in the issuance of 35,000 shares based on the current price of the Company's stock on the date of exercise. The aggregate intrinsic value of options exercised during the year ending September 30, 2010 and 2009 was \$779,546 and \$52,500, respectively.

Total compensation cost charged against operations under the plan for employees was \$840,780 and \$1,609,093 for the year ended September 30, 2010 and 2009, respectively. These costs are classified under salaries and benefits expense. Total compensation cost charged against operations under the plan for directors and consultants was \$627,294 and \$464,953 for the year ended September 30, 2010 and 2009, respectively. These costs are classified under other general and administrative expenses.

As of September 30, 2010, total unrecognized compensation expense related to options was \$153,892 and the related weighted-average period over which it is expected to be recognized is approximately 0.27 years. The aggregate intrinsic value of options outstanding and exercisable as of September 30, 2010, before applicable income taxes, was \$3,072,670 and \$2,452,076, respectively, based on our closing price of \$1.17 per common share at September 30, 2010.

NOTE 16 – DISCONTINUED OPERATIONS:

In September 2010, the Company ceased its drilling service operations in Mexico and moved all of the serviceable assets in Mexico to the United States for future use. The results of operations for the Company's Mexican subsidiary, World Wide Exploration, have been reported in discontinued operations for all periods presented.

The following table details selected financial information included in the loss from discontinued operations in the consolidated statements of operations for the years ended September 30, 2010 and 2009:

	2010	2009
Revenues	\$ 1,978,270	\$ 4,331,005
Cost of revenues	(2,850,142)	(3,879,272)
Operating expenses	(428,549)	(698,016)
Severance expense	(106,579)	-
Write-down of property and equipment held for sale	(132,993)	-
Write-down of inventory held for sale	(229,026)	-
Foreign exchange gain (loss)	142,654	(74,779)
Interest income	4,069	17,601
Interest expense	(1,265)	(20,760)
Other income	5,909	-
Income tax benefit	-	145,089
Loss from discontinued operations, net of tax	\$ <u>(1,617,652)</u>	\$ <u>(179,132)</u>

The consolidated balance sheet of the Company at September 30, 2010 has assets held for sale of \$319,291 which includes \$228,641 in inventory and \$90,650 in property and equipment resulting from the discontinued operations.

TIMBERLINE RESOURCES CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2010

NOTE 16 – DISCONTINUED OPERATIONS, (continued):

Cash flows from discontinued operations, included in the Company's consolidated statements of cash flows for the years ending September 30, 2010 and 2009 are as follows:

	2010	2009
Cash flows from operating activities	\$ (159,976)	\$ 131,699
Cash flows from financing activities	-	(24,869)
Cash flows from investing activities	(9,363)	(15,679)
Total cash flows from discontinued operations	\$ (169,339)	\$ 91,151

NOTE 17 – SEGMENT INFORMATION:

The Company has two operating segments at September 30, 2010 and 2009: drilling revenues from Timberline Drilling, and Timberline Resource's exploration activities. As a result of the closure of our drilling service operations in Mexico during the year ended September 30, 2010, segment information for the periods presented in the table below has been adjusted to reflect the discontinued operations.

Segment information for the years ended September 30, 2010 and 2009 is as follows:

	2010	2009
Revenues from continuing operations:		
Timberline Resources	\$ -	\$ -
Timberline Drilling	21,813,435	13,242,093
Elimination of intersegment revenues	(1,080,098)	-
Total revenues from continuing operations	\$ 20,733,337	\$ 13,242,093
Income (loss) before income taxes from continuing operations:		
Timberline Resources	\$ (6,251,145)	\$ (5,997,234)
Timberline Drilling	1,709,938	(1,132,262)
Loss before income taxes from continuing operations	\$ (4,541,207)	\$ (7,129,496)
Identifiable assets:		
Timberline Resources	\$ 17,577,156	\$ 1,323,051
Timberline Drilling	13,172,598	9,997,792
Discontinued operations	518,775	2,703,384
Total identifiable assets	\$ 31,268,529	\$ 14,024,227
Depreciation and amortization from continuing operations:		
Timberline Resources	\$ 50,483	\$ 36,492
Timberline Drilling	1,217,660	1,037,670
Total depreciation and amortization from continuing operations	\$ 1,268,143	\$ 1,074,162
Expenditures for additions to property and equipment:		
Timberline Resources	\$ -	\$ -
Timberline Drilling	2,567,603	463,523
Discontinued operations	31,168	20,979
Total expenditures for additions to capital assets	\$ 2,634,771	\$ 484,502

Separate management of each segment is required because each business unit is subject to different marketing, production, and technology strategies.

TIMBERLINE RESOURCES CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2010

NOTE 17 – SEGMENT INFORMATION, (continued):

During the years ended September 30, 2010 and 2009, revenue from transactions with one customer amounted to 10% or more of our consolidated revenues. Newmont accounted for revenue of \$19,283,298 and \$11,888,386 for the years ending September 30, 2010 and 2009, respectively.

The assets of Timberline Resources are located in the United States. The assets of Timberline Drilling are also located in the United States and their revenues are derived from drilling contracts in the United States. Timberline Resources is not an operating entity at this point insofar as they are not generating revenues from the sales of their properties, but they are actively exploring several properties for their mining potential.

NOTE 18 – COMMITMENTS AND CONTINGENCIES:

Real Estate Lease Commitments

The Company has real estate lease commitments related to its main office in Coeur d’Alene, Idaho, facilities in Butte, Montana and Eureka, Nevada, and offices and a shop of Timberline Drilling in Coeur d’Alene, Idaho. Total office and storage rental expense aggregated \$205,116 and \$284,015 for the years ended September 30, 2010 and 2009, respectively.

Annual lease obligations until the termination of the leases are as follows:

For the year ending September 30,

2011	\$174,973
2012	\$101,220
2013	\$ 34,305
2014	\$ -
2015	\$ -

Environmental Contingencies

The Company has, in past years, been engaged in mining in northern Idaho, which is currently the site of a federal Superfund cleanup project. Although the Company is no longer involved in mining in this or other areas at present, the possibility exists that environmental cleanup or other environmental restoration procedures could remain to be completed or mandated by law, causing unpredictable and unexpected liabilities to arise. At the date of these financial statements, the Company is not aware of any environmental issues or litigation relating to any of its current or former properties.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

ITEM 9A. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

At the end of the period covered by this Annual Report on Form 10-K, an evaluation was carried out under the supervision of and with the participation of the Company's management, including the Chief Executive Officer and Chief Financial Officer, Randal Hardy ("CEO/CFO") and Chief Accounting Officer, Craig Crowell, ("CAO"), of the effectiveness of the design and operations of the Company's disclosure controls and procedures (as defined in Rule 13a – 15(e) and Rule 15d – 15(e) under the Exchange Act). Based on that evaluation the CEO/CFO and the CAO have concluded that the Company's disclosure controls and procedures were adequately designed and effective in ensuring that: (i) information required to be disclosed by the Company in reports that it files or submits to the Securities and Exchange Commission under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in applicable rules and forms and (ii) material information required to be disclosed in our reports filed under the Exchange Act is accumulated and communicated to our management, including our CEO/CFO and CAO, as appropriate, to allow for accurate and timely decisions regarding required disclosure.

Internal Control over Financial Reporting

The management of Timberline is responsible for establishing and maintaining adequate internal control over financial reporting for the Company (including its consolidated subsidiaries) and all related information appearing in the Company's Annual Report on Form 10-K. The Company's internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with accounting principles generally accepted in the United States of America. Internal control over financial reporting includes those policies and procedures that:

1. pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of our assets;
2. provide reasonable assurance that the transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that our receipts and expenditures are being made only in accordance with the authorization of management and/or of our Board of Directors; and
3. provide reasonable assurance regarding the prevention or timely detection of any unauthorized acquisition, use or disposition of our assets that could have a material effect on our financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness in future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management conducted an evaluation of the design and operation of the Company's internal control over financial reporting as of September 30, 2010 based on the criteria in a framework developed by the Company's management pursuant to and in compliance with the principles and framework of the Committee of Sponsoring Organizations of the Treadway Commission. This evaluation included review of the documentation of controls, evaluation of the design effectiveness of controls, walkthroughs of the operating effectiveness of controls and a conclusion on this evaluation. Based on this evaluation, management has concluded that the Company's internal control over financial reporting was effective as of September 30, 2010.

This Report does not include an attestation report of the Company's registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by our registered public accounting firm pursuant to Section 404(c) of the Sarbanes-Oxley Act, as amended, which permit us as an issuer that is neither a "large accelerated filer" or an "accelerated filer" to provide only management's report in this Annual Report on Form 10-K.

Changes in Internal Controls over Financial Reporting

There were no changes in the Company's internal control over financial reporting (as defined in Rule 13a-15(f) or 15d-15(f)), that occurred during the Company's fourth fiscal quarter ended September 30, 2010 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

ITEM 9B. OTHER INFORMATION

None.

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS, AND CORPORATE GOVERNANCE

Reference is made to the information set forth under the captions “Election of Directors” and “Executive Officers” in our definitive proxy statement to be filed with the Securities and Exchange commission pursuant to Regulation 14A, which information is incorporated by reference to this Annual Report on Form 10-K.

ITEM 11. EXECUTIVE COMPENSATION

Reference is made to the information set forth under the captions “Election of Directors” and “Executive Officers” in our definitive proxy statement to be filed with the Securities and Exchange commission pursuant to Regulation 14A, which information is incorporated by reference to this Annual Report on Form 10-K.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDERS MATTERS

Reference is made to the information set forth under the captions “Security Ownership of Principal Shareholders and Management” in our definitive proxy statement to be filed with the Securities and Exchange commission pursuant to Regulation 14A, which information is incorporated by reference to this Annual Report on Form 10-K.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS AND DIRECTOR INDEPENDENCE

Reference is made to the information set forth under the caption “Certain Transactions” in our definitive proxy statement to be filed with the Securities and Exchange commission pursuant to Regulation 14A, which information is incorporated by reference to this Annual Report on Form 10-K.

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

Reference is made to the information set forth under the captions “Audit Committee Report” in our definitive proxy statement to be filed with the Securities and Exchange commission pursuant to Regulation 14A, which information is incorporated by reference to this Annual Report on Form 10-K.

PART IV

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

Documents Filed as Part of Report

Financial Statements

The following Consolidated Financial Statements of the Corporation are filed as part of this report:

1. Report of Registered Public Accounting Firm dated December 16, 2010.
2. Consolidated Balance Sheets—At September 30, 2010 and 2009.
3. Consolidated Statements of Operations—Years ended September 30, 2010 and 2009.
4. Consolidated Statements of changes in Stockholders’ Equity—Years ended September 30, 2010 and 2009.
5. Consolidated Statements of Cash Flows—Years ended September 30, 2010 and 2009.
6. Notes to Consolidated Financial Statements.

See “Item 8. Financial Statements and Supplementary Data”.

TABLE OF CONTENTS

Exhibit No.	Description of Document
3.1	Certificate of Incorporation of the Registrant (9)
3.2	By-Laws of the Registrant (9)
4.1	Specimen of the Common Stock Certificate (1)
4.2	Form of Warrant for November 2009 Private Placement
4.3	Convertible Note between the Company and Ron and Stacey Guill (10)
4.4	Term Note between the Company and Small Mine Development, LLC (10)
10.1	Hecla Agreement//Joint Venture Agreement for Snowstorm, Idaho (1)
10.2	Snowshoe Mining Co. Lease//Mineral Lease Property at Snowstorm, Idaho (1)
10.3	Western Goldfields, Inc. Lease//Mineral Lease with Western Goldfields, Inc./Claim at the Snowstorm Project, Idaho (1)
10.4	P. Dirksen Agreement/Current Consulting Agreement (1)
10.5	2005 Equity Incentive Plan approved at the September 23, 2005 Annual Meeting of Shareholders (1)
10.6	2/1/06 Memorandum of Royalty Deed and Agreement between Hecla Mining Co. and the Registrant (2)
10.7	2/1/06 Quitclaim Deed and Assignment between Hecla Mining Co. and the Registrant (3)
10.8	Amended 2005 Equity Incentive Plan approved at the September 22, 2006 Annual Meeting of Shareholders (4)
10.9	5/1/06, Employment Agreement with VP Paul Dirksen (5)
10.10	Assignment and Assumption Agreement dated July 19, 2007 between the Registrant and Butte Highlands Mining Company (6)
10.11	Promissory Note, dated June 27, 2008, entered into between Timberline Resources Corporation and Auramet Trading, LLC.(7)
10.12	Severance Agreement, dated March 10, 2008 among Timberline Resources Corporation, Douglas Kettle and David and Margaret Deeds.(7)
10.13	Amendment No. 1 to Timberline Resources Corporation's Amended 2005 Equity Incentive Plan (8)
10.14	Agreement and Plan of Merger between Timberline Resources Corporation, an Idaho corporation ,and Timberline Resources Corporation, a Delaware corporation, date August 22, 2008 (9)
10.15	Pledge Agreement between the Company and Ron and Stacey Guill. (10)
10.16	Security Agreement between the Company and Ron and Stacey Guill.(10)
10.17	Credit Agreement between the Company and Small Mine Development, LLC. (10)
10.18	Pledge Agreement between the Company and Small Mine Development, LLC. (10)
10.19	Right of First Refusal between the Company and Small Mine Development, LLC. (10)
10.20	Settlement Agreement with John Swallow, dated October 5, 2009
10.21	Operating Agreement with Highland Mining, LLC, dated July 22, 2009 (Note that parts of this agreement have been redacted pursuant to a Confidential Treatment Request filed with the Commission concurrently herewith)
10.22	Settlement Agreement with Jefferies & Co. dated July 14, 2009
10.23	Amended Employment Agreement of Mr. Paul Dirksen, dated December 29, 2008 (11)
10.24	Amended Employment Agreement of Mr. Randal Hardy dated December 29, 2008 (11)
10.25	Amended Employment Agreement of Mr. John Swallow dated December 29, 2008 (11)
10.26	Arrangement Agreement between the Company and Staccato Gold dated March 22, 2010 (12)
10.27	Form of Support Agreement between the Company and officers and directors of Staccato Gold (12)
10.28	Loan Amendment Agreement between the Company and Small Mine Development, LLC dated June 21, 2010 (13)
14	Code of Ethics (2)
21	List of Subsidiaries
23.1	Consent of Decoria, Maichel & Teague
31.1	Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (Rules 13a-14 and 15d-14 of the Exchange Act)
31.2	Certification of Chief Accounting Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (Rules 13a-14 and 15d-14 of the Exchange Act)
32.1	Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. 1350)
32.2	Certification of Chief Accounting Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. 1350)

(1) Incorporated by reference to the Company's Form 10SB as filed with the Securities Exchange Commission on September 29, 2005.

(2) Incorporated by reference to Exhibit 10.3 to the Company's Form 8-K as filed with the Securities Exchange Commission on February 6, 2006.

(3) Incorporated by reference to Exhibit 10.2 to the Company's Form 8-K as filed with the Securities Exchange Commission on February 6, 2006.

(4) Incorporated by reference Exhibit A to the Company's Schedule DEF14A (Proxy Statement) as filed with the Securities and Exchange Commission on September 8, 2006

(5) Incorporated by reference to the Company's Form 10KSB as filed with the Securities Exchange Commission on January 16, 2007.

(6) Incorporated by reference to the Company's Form 8-K as filed with the Securities and Exchange Commission on July 23, 2007.

(7) Incorporated by reference to the Company's Form 8-K as filed with the Securities and Exchange Commission on July 3, 2008..

(8) Incorporated by reference to the Company's Form 8-K as filed with the Securities and Exchange Commission on August 26, 2008.

(9) Incorporated by reference to the Company's Form 8-K as filed with the Securities and Exchange Commission on August 29, 2008.

(10) Incorporated by reference to Ron and Stacey Guill's Schedule 13-D as filed with the Securities and Exchange Commission on December 24, 2008.

(11) Incorporated by reference to the Company's Form 8-K as filed with the Securities and Exchange Commission on January 12, 2009.

(12) Incorporated by reference to the Company's Form 8-K as filed with the Securities and Exchange Commission on March 29, 2010.

(13) Incorporated by reference to the Company's Form 10-Q as filed with the Securities and Exchange Commission on August 11, 2010.

SIGNATURES

In accordance with Section 13 or 15(d) of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized:

TIMBERLINE RESOURCES CORPORATION

<u>/s/ Randal Hardy</u>	Chief Executive Officer, Chief Financial Officer and Director (Principal Executive and, Financial Officer)	December 17, 2010
Randal Hardy		
<u>/s/ Craig Crowell</u>	Chief Accounting Officer (Principal Accounting Officer)	December 17, 2010
Craig Crowell		

In accordance with the requirements of the Securities Exchange Act of 1934, as amended, this Annual Report on Form 10-K was signed by the following persons in the capacities on the dates stated:

<u>/s/ Randal Hardy</u>	Chief Executive Officer, Chief Financial Officer and Director (Principal Executive and Financial Officer)	December 17, 2010
Randal Hardy		
<u>/s/ Craig Crowell</u>	Chief Accounting Officer (Principal Accounting Officer)	December 17, 2010
Craig Crowell		
<u>/s/ Paul Dirksen</u>	Director, Executive Chairman of the Board, and Vice-President, Exploration	December 17, 2010
Paul Dirksen		
<u>/s/ Vance Thornsberry</u>	Director	December 17, 2010
Vance Thornsberry		
<u>/s/ Eric Klepfer</u>	Director	December 17, 2010
Eric Klepfer		
<u>/s/ Ron Guill</u>	Director	December 17, 2010
Ron Guill		
<u>/s/ James H. Moore</u>	Director	December 17, 2010
James H. Moore		
<u>/s/ Robert Martinez</u>	Director	December 17, 2010
Robert Martinez		
<u>/s/ David Poynton</u>	Director	December 17, 2010
David Poynton		

SETTLEMENT AGREEMENT

This Agreement is made as of the 5th day of Oct., 2009, by and between Timberline Resources Corporation (the "Company") and John Swallow, a former director and former executive of the Company (the "Insider") in connection with a claim arising under Section 16(b) of the Securities Exchange Act of 1934.

WHEREAS, based on its review of certain transactions in the Company's common stock while the Insider was a director and executive of the Company, as detailed on Schedule A hereto (the "Transactions"), the Company informed the Insider of its belief that he may have realized recoverable profits in connection with the Transactions which are recoverable by the Company under Section 16(b) of the Securities and Exchange Act of 1934, as amended (the "Claim").

WHEREAS, the Insider has agreed to pay to the Company \$ 38,900.00 in full satisfaction of the Claim (the "Payment"), such amount calculated as shown on Schedule B hereto. In relation to any amounts being claimed as a deduction from the gross profits realized by any direct costs incurred by the Insider in connection with the trades comprising the Transaction, including brokerage commissions, transfer taxes, and other fees and expenses incurred in connection with the Transaction, the Insider has provided the Company with documentation satisfactory to the Company regarding the actual amounts of such direct costs.

WHEREAS, the Company has agreed that the Payment will satisfy the Claim in full.

NOW, THEREFORE, in consideration of the mutual covenants contained herein, and intending to be legally bound, the parties hereby agree as follows:

1. The Insider will pay to the Company, simultaneously with the execution of this Agreement, \$ 38,900.00 in full settlement and satisfaction of the Claim and the Company hereby agrees that upon receipt of the Claim it will not take any further action against the Insider in connection with the Claim or matters relating thereto, and will keep confidential all matters relating to the Claim and this Agreement, except to the extent that disclosure of any such matter may be required by law or to settle any claim for attorney fees that may lawfully arise in relation to a securityholder action under Section 16(b) in regard to the Claim, pursuant to paragraph 2 below.

2. The Company agrees to pay any attorney fees in settlement of any securityholder action under Section 16(b) in regard to the Claim that are required by law to be paid.

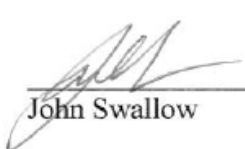
IN WITNESS WHEREOF, the parties have executed this Agreement as of the date set forth above.

TIMBERLINE RESOURCES CORPORATION

By: 

Name: RANDAL L. HARDY

Title: CEO


John Swallow

* Note on Redacted Material: Sections under the heading "Proposed Rates", "SMD Personnel", and "Proposed Work Schedule" in Exhibit B to this Agreement have been omitted pursuant to a Confidential Treatment Request ("Request") Timberline Resources Corporation filed with the United States Securities and Exchange Commission ("SEC") concurrently with the filing of the Form 10-K to which this Agreement is an exhibit. The omitted material has been filed separately with the SEC as part of the request. The place of omitted provisions are indicated below as "REDACTED". Two pages contain omitted provisions.
Exhibit 10.21

**OPERATING AGREEMENT
OF
BUTTE HIGHLANDS JV, LLC**

I. FORMATION OF COMPANY.

1. **Formation.** On May 8, 2009, the Company was formed by filing the Articles of Organization with the Idaho Secretary of State in accordance with and pursuant to the Act.
2. **Name.** The name of the Company is Butte Highlands JV, LLC.
3. **Principal Place of Business.** The principal place of business of the Company is located at 967 East ParkCenter Boulevard, PMB 174, Boise, Idaho 83706.
4. **Registered Agent and Office.** The Company's registered agent and office in Idaho is Ron Guill, 967 East ParkCenter Boulevard, Boise, Idaho, 83706. The Company's registered agent and office in Montana is David Bjornson, 2809 Great Northern Loop, Suite 100, Missoula, Montana 59808.
5. **Definition of Terms.** Capitalized terms used in this Agreement shall have the meanings set forth in Section XV hereof or in the applicable provisions in which the terms are used.
6. **Title to Property.** All real and personal property owned by the Company shall be property of the Company and no Member shall have any ownership interest in such property in his or her individual name or right, and each Member's Interest in the Company shall be considered personal property for all purposes.

II. PURPOSE OF COMPANY BUSINESS. The Company is organized solely to own, explore, develop, process and sell mined ore from property owned, leased or in which the Company or a Member owns or leases or has an interest within five (5) miles of the Butte Highlands portal, which portal is located in Silver Bow County, Montana (collectively the "Property").

III. TERM. The term of the Company commenced on the date its Articles of Organization were filed with the Idaho Secretary of State and shall continue in perpetuity, unless sooner terminated pursuant to this Agreement.

IV. MEMBERS, INTERESTS AND CAPITAL CONTRIBUTIONS.

1. **Members and Initial Contribution.** The initial Members of the Company are Highland Mining, LLC ("Highland"), and Timberline Resources Corporation ("Timberline"). The U.S. mail addresses, email addresses, facsimile and phone numbers, as applicable, and the Percentage Interests of each Member of the Company are set forth on Exhibit "A". Timberline and Highland shall contribute the Property to the Company within thirty (30) days of the date of this Agreement. For the avoidance of doubt, the Property shall include all interests, such as unpatented and patented claims, leased property, and fee interests. Within the same time period, Highland shall enter into the Loan (defined below).

2. **No Additional Contributions.** Except as provided in this Agreement, no Member shall be required to make any additional contributions to the capital of the Company. No Member shall be entitled to interest on any Capital Contribution or on such Member's Capital Account. The Members may make additional Capital Contributions to the Company at such time and in such amounts as may be approved by the Management Committee.

3. **Limitation on Liability of Members.** No Member of the Company shall be personally liable for any debt, obligation or liability of the Company.

V. **COMPANY MANAGEMENT.**

1. **Management.**

A. Until the Members reach "Parity," the Company shall be managed by such manager or managers as Highland shall appoint in its sole discretion. Until the Members reach Parity, the Management Committee shall have an advisory role only, and shall have no authority. Subject to the terms of this Agreement, until the Members reach Parity, the manager(s) shall have full and complete authority, power and discretion to manage and control the business, affairs and properties of the Company, to make all decisions regarding those matters, and to perform any and all other activities customary or incident to the management of the Company's business. No Member shall individually have any authority to act for, or assume any obligation or responsibility on behalf of, any other Member or the Company.

B. After the Members reach "Parity," the Members shall direct, manage and control the business of the Company through the Management Committee. Subject to the terms of this Agreement, the Management Committee shall have full and complete authority, power and discretion to manage and control the business, affairs and properties of the Company, to make all decisions regarding those matters, and to perform any and all other activities customary or incident to the management of the Company's business. No Member shall individually have any authority to act for, or assume any obligation or responsibility on behalf of, any other Member or the Company.

2. **Managers.**

A. Number and Qualifications of Managers. The number of managers shall be the number appointed by Highland and acting as such from time to time, but shall not be less than one (1) nor more than three (3). Managers may be individuals or entities, and need not be members of the Company. The term of all Managers shall terminate when the Members reach Parity. Thereafter, the management of the Company shall be through and by the Management Committee subject to this Agreement. The initial Manager shall be Ron Guill.

B. Appointment of Managers. Managers shall be appointed by Highland. A manager shall serve until the manager's earlier death, resignation, or removal, or Parity is reached.

C. Authority. Subject to restrictions that may be imposed from time to time by the managers or Highland, each manager shall be an agent of the Company with authority to bind the Company in the ordinary course of its business. The managers shall have

no authority to bind the Company as to the following matters without first obtaining approval by vote of the members:

- 1) Sale, lease, exchange, mortgage, pledge, or other transfer or disposition of all or substantially all the assets of the Company;
- 2) Merger of the Company with another entity;
- 3) Amendment to the Articles of Organization;
- 4) Incurrence of indebtedness by the Company other than in the ordinary course of business; or
- 5) A change in the nature of the business of the Company.

D. Other Activities Managers may have other business interests and may engage in other activities in addition to those relating to the Company. This Section does not change each manager's duty to act in a manner that the manager reasonably believes to be in the best interests of the Company.

E. Meetings; Notices; Quorum; Voting. Meetings of the managers may be called by any manager. Meetings shall be held at the place fixed by the managers or, if no such place has been fixed, at the principal office of the Company. Oral or written notice of the date, time, and place of any meeting shall be given at least twenty-four (24) hours in advance. Written notice may be delivered personally, given by facsimile or other form of wire communication, or by mail or private carrier, to each manager's business or home address. Written notice shall be effective at the earliest of the following: (a) when received, (b) when sent by facsimile or other form of wire communication, or (c) two business days after being mailed. A majority of the managers shall constitute a quorum. Each manager shall be entitled to one vote. The matter submitted to a vote of the managers shall be deemed approved if the votes in favor exceed those against the matter..

F. Resignation. A manager may resign at any time by delivering written notice to the other managers or to Highland. The resignation is effective when the notice is effective under the Act, unless the notice specifies a later effective date. Once delivered, a notice of resignation is irrevocable unless revocation is permitted by the managers. The resignation of a manager who is also a member shall not affect the manager's rights as a member and shall not constitute a withdrawal of the member.

G. Removal of a Manager. Highland may remove one or more managers with or without cause. A manager may be removed by Highland only at a meeting called for the purpose of removing the manager and the meeting notice must state that the purpose, or one of the purposes, of the meeting removal of the manager.

H. Vacancy. If a vacancy occurs in the number of managers, Highland shall fill the vacancy. A vacancy that will occur at a specific later date may be filled before the vacancy occurs but the new manager may not take office until the vacancy occurs.

I. **Salaries.** The salaries and other compensation of the managers shall be reasonable and fixed from time to time by Highland. A manager shall not be precluded from receiving a salary because the manager is also a Member.

J. **Other Agents.** The managers may, by vote, authorize any agent to enter into any lawful contract or to otherwise act on behalf of the Company. Such authority may be general or be confined to specific instances.

3. **Management Committee.** When the Members reach "Parity," a Management Committee shall be formed to manage the Company. The Management Committee will be comprised of four (4) Representatives, two (2) of which shall represent and be designated by Highland and two (2) by Timberline, unless there is a Change of Control of a Member and an additional representative is added as provided in Section XIII.4. Highland and Timberline may, by written notice to the other, remove and designate a replacement Representative at any time. The operations, meetings and deliberations of the Management Committee shall be governed by the provisions set forth in this Agreement. The Management Committee shall direct, manage and control the business and affairs of the Company and may in connection therewith, exercise or delegate any of the rights, powers and privileges which the Company might exercise to further the purposes thereof, subject to this Agreement. Except as otherwise provided herein, any act of the Company properly approved or authorized by the Management Committee shall be binding upon the Members.

4. **Limitation on Liability of the Representatives.** None of the Representatives shall be liable to the Company or any Member for any act or omission performed or omitted by it in good faith pursuant to the authority granted by this Agreement, other than an act constituting fraud, gross negligence, willful or wanton misconduct, or breach of fiduciary obligation in the performance of its duty to the Company or otherwise in breach of this Agreement.

5. **Indemnification of the Representatives.** The Company shall indemnify and hold harmless each Representative and any Manager of the Company from and against any loss, expense, damage, or injury which such Person may suffer or sustain by reason of any actual or alleged acts or omissions conducted on behalf of the Company or in furtherance of the interests of the Company (including any judgment, award, settlement, and any reasonable attorneys' fees and other costs or expenses incurred in connection with the defense of any actual or threatened action, proceeding, or claim). The foregoing shall apply only if the conduct of the Person to be indemnified did not constitute gross negligence and if such Person acted in good faith and in a manner such Person reasonably believed to be in the best interests of the Company and, in the case of a criminal proceeding, had no reasonable cause to believe his or her conduct was unlawful. The termination of any action, suit, or proceeding by judgment, order, settlement, conviction, or upon a plea of nolo contendere or its equivalent shall not, of itself, create a presumption that the Person to be indemnified did not act in good faith and in a manner which he or she reasonably believed to be in, or not opposed to, the best interests of the Company, or that such Person reasonably believed to be unlawful.

6. **The Staff.** The Management Committee or the Operations Manager may, after the Members reach Parity and subject to Section V.8, designate and determine such positions and offices of the Company from time to time as they may consider appropriate or desirable for the furtherance of the purposes of the Company, and may hire such individuals to fill such positions upon such terms and conditions as they may then consider appropriate or desirable.

7. **Tax Matters Member.** Highland shall be the tax matters partner within the meaning of Section 6211 et seq. of the Code. The appointment of the Company's tax matters partner may

be revoked only upon the act of the Management Committee pursuant to Section V.8. The tax matters partner shall have authority to take all action necessary or proper with respect to any action required or permitted to be taken in determining any Company tax item under the Code, and shall assist the Operations Manager with tax returns pursuant to Section XI.3.

8. **Major Actions.** After the Members have reached Parity, none of the following actions shall be taken by the Company or by any Member or other Person on behalf of or for the account of the Company, unless first approved by the Management Committee pursuant to Section VI:

- A. Any consolidation or liquidation of the Company.
- B. Any amendment to the Operating Agreement or other charter documents of the Company.
- C. Capital expenditures in excess of \$1,000,000, individually or in the aggregate, for any fiscal year.
- D. Approval or authorization of the incurrence of indebtedness for borrowed money.
- E. Selection of auditors and general counsel, and the settlement of litigation .
- F. Any loan, transaction or contract with Members or their Affiliates, other than de minimis product purchases made in the ordinary course of business.
- G. Any change in the distribution of earnings.
- H. Selection and supervision of executive officers, managers and other key personnel.
- I. Setting of policies and guidelines on employee compensation and benefits, as well as any change in compensation (including benefits) for (a) hourly personnel that is outside of the above policies and guidelines, and for (b) other personnel that is outside of normal industry ranges for such personnel.
- J. Approval of the Company's financial reporting requirements, annual budget, annual business plans, and any amendments thereto.
- K. Any contract (including, but not limited to, any lease or other oral or written agreement) or expenditure of money exceeding \$1,000,000.
- L. Causing the Company to become a surety, guarantor or endorser (except checks and drafts for deposit to the Company's accounts).
- M. The Company's acquisition of any ownership interest in any corporation or other legal entity or business enterprise, or the creation of any partnership or other legal entity in which the Company is or will be a partner, shareholder, member or similar participant.
- N. Any sale, lease or other transfer of any assets of the Company .

O. Creation or incurrence of any mortgage, pledge, lien, charge or encumbrance upon any of the property or assets now owned or hereafter acquired by the Company.

P. Approval of federal, state and other income tax returns.

9. **Enforcement of Contract Rights.** Notwithstanding anything in this Agreement to the contrary, after the Members reach Parity, when a Member is a party (either directly or through any Affiliate) to any contract with the Company, the rights of the Company thereunder shall be enforceable solely by the Representatives appointed by the other Member. Prior to reaching Parity, the Members acknowledge that a related party of Highland will be developing and operating the Property.

VI. **MEETINGS OF REPRESENTATIVES.**

1. **Quarterly Meetings.** The Management Committee shall have regular quarterly meetings.

2. **Special Meetings.** Special meetings of the Management Committee may be called at the request of at least two (2) Representatives for any purpose or purposes.

3. **Place of Meetings.** Meetings of the Management Committee shall be conducted at the principal business office of the Company, unless the Representatives unanimously designate such other place of meeting. The Representatives may participate in and hold a meeting by conference telephone or similar communications equipment by means of which all Persons participating in the meeting can hear each other. Such participation shall constitute attendance and presence in person at such meeting, except where a Person participates in the meeting for the express purpose of objecting to the transaction of any business on the ground that the meeting is not lawfully called or convened.

4. **Notice of Meetings.** No notice need be given to the Management Committee of regular quarterly meetings for which the Management Committee has previously designated a time and place for the meeting. Except as provided in Sections VI.5, VI.8, and VI.9, written notice stating the place, date and hour of any special meeting and the purpose or purposes for which the meeting is called, shall be prepared by the Representatives calling such special meeting and delivered not less than ten (10) nor more than sixty (60) days before the date of the meeting. Delivery shall be sufficient if made personally, by mail, e-mail, overnight courier service, telecopy or telegram to each Representative entitled to vote at such meeting.

5. **Meeting of All Representatives.** Should all of the Representatives meet at any time and place and consent to the holding of a meeting at such time and place, such meeting shall be valid without notice and lawful action may be thereat.

6. **Quorum.** Three (3) Representatives must be present to constitute a quorum for the transaction of business at any meeting of the Representatives.

7. **Manner of Acting.** The affirmative vote of three (3) Representatives shall be the act of the Members.

8. **Action by Management Committee Without a Meeting.** Any action required or permitted to be taken at a meeting of the Management Committee may be taken without a meeting if the action is evidenced by one or more written consents describing the action taken, signed by all the Representatives entitled to vote. Unless the consent specifies a different

effective date, action taken under this Section is effective when all such Representatives have signed the consent. A photostatic, facsimile or similar reproduction of a writing signed by a Representative shall be regarded as signed by the Representative for purposes of this Section.

9. **Waiver of Notice.** When any notice is required to be given to any Representative, a waiver thereof in writing signed by the person entitled to such notice, whether before, at or after the time stated therein, shall be equivalent to the giving of such notice.

10. **Proxies.** A Representative entitled to vote may vote either in person or by proxy executed in writing by the Representative. A photostatic, facsimile or similar reproduction of a writing signed by the Representative shall be regarded as duly executed for purposes of this Section.

VII. **OPERATIONS MANAGEMENT.**

1. **Appointment.** Once the Members reach Parity, the day to day operations of the Company shall be managed by an Operations Manager and a Controller. The Management Committee shall at all times have the right to appoint and remove the Operations Manager and Controller for the Company. The Operations Manager shall manage and direct the overall operations of the Company's business and facilities, and the Controller shall be responsible for the supervision and control of the financial and fiscal affairs of the Company, in each case pursuant to directions by the Management Committee. This Section VII notwithstanding, neither such officer shall take any action, make any expenditure or incur any obligation on behalf of the Company with respect to a matter within the scope of any of the major decisions set forth in Section V.8 unless such major decision has been approved by the Management Committee.

2. **Operating Plan.** The Operations Manager and Controller shall annually (or more or less frequently as approved by the Management Committee) prepare and submit for consideration and approval by the Management Committee an Operating Plan for the upcoming year (or other such period requested by the Management Committee). As used herein: the term "Operating Plan" means a description in reasonable detail of the activities to be carried out and the objectives of the Company, including a budget, for a year or any longer period. When approved by the Management Committee, the Operations Manager and Controller shall implement the Operating Plan and shall be authorized to make the expenditures and to incur the obligations provided for in the Operating Plan without the need for further approval by the Management Committee, subject to Section V.8..

3. **Additional Duties of the Operations Manager.**

A. The Operations Manager shall be responsible for managing the day-to-day business and affairs of the Company. The Operations Manager shall have the authority, on behalf of and in the name of the Company, to sign all documents and to make all expenditures and incur all obligations reasonably necessary for the management of the day-to-day business and affairs of the Company.

B. The Operations Manager shall, at the Company's expense, implement or cause to be implemented all decisions approved by the Management Committee and conduct or cause to be conducted the day-to-day business and affairs of the Company in accordance with and as limited by the Operating Plan and this Agreement, including the following:

- 1) Purchase or otherwise acquire all supplies, equipment, utilities, labor and logistics services required for the Company's operations;
- 2) Retain or employ and coordinate the services of all employees, as well as all leased or contracted employees and other Persons necessary or appropriate to carry out the purposes of the Company;
- 3) Apply for all permits, licenses and approvals necessary to the Company's operations;
- 4) Notify promptly the Management Committee of any alleged violations of applicable federal, state and local laws and regulations;
- 5) Prepare and file all reports or notices required for the Company's operations; and
- 6) Sign and execute contracts on behalf of the Company.

4. **Additional Duties of the Controller.** The Controller shall, at the Company's expense, implement all fiscal policies of the Company and generally oversee and be responsible for the financial management and recordkeeping of the Company in compliance with and subject to the Operating Plan and this Agreement. These duties will include the following:

- A. Review and, if appropriate, approve for payment all debts incurred in the operation of the Company and contained in an approved Operating Plan;
- B. Prepare and maintain all financial, accounting, tax and other books and records of the Company in accordance with Section XI;
- C. Timely pay all insurance premiums, debts and other obligations of the Company provided for in the approved Operating Plan;
- D. Maintain a separate bank account or accounts in the name of the Company, with such bank or banks selected by the Management Committee, in which there shall be deposited all Company funds including capital contributions and gross receipts from activities of the Company; and
- E. Make, when permitted or required by this Agreement, periodic distributions of cash or property to the Members in accordance with the provisions of this Agreement;

5. **Limitation on Liability.** Neither the Operations Manager nor the Controller shall be in default of any duty under this Section VII if his or her failure to perform results from the failure of any Member to perform acts or to contribute amounts required by this Agreement. Neither such officer shall be liable to either Member for any act or omission in his capacity as Operations Manager or Controller, as the case may be, and within the scope of his authority, except to the extent resulting in damage or loss caused by his willful misconduct.

VIII. **DEVELOPMENT.**

1. Development. The Members acknowledge that the Company shall enter into an agreement with Small Mine Development, LLC, an Idaho limited liability company ("SMD") for the development of the Property. The agreement between the Company and SMD shall be substantially in the form attached hereto as Exhibit B, which is attached hereto and made a part hereof (the "SMD Agreement."). The Members agree and acknowledge that Ron Guill, as manager of the Company, is authorized to sign and execute any such agreement, and any modifications or amendments thereto, on behalf of the Company.

2. Other Services. The Company and Highland will enter into the loan agreement, promissory note and other loan documents substantially in the form attached hereto, or to be attached hereto within thirty (30) days of the date of this Agreement, as Exhibit "C" (the "Loan Documents"). The Members agree and acknowledge that Ron Guill as manager of the Company is authorized to sign and execute the Loan Documents and any and all documents necessary or convenient thereto. The Loan Documents will provide, among other things, that the loan evidenced by the Loan Documents (the "Loan") may be called any time at or after the point of a production decision, payable under the terms of this Agreement, and that Ron Guill as manager is authorized to make such decision in his sole discretion as manager of the Company.

IX. DISTRIBUTIONS AND ALLOCATIONS.

1. Allocation of Profits and/or Losses.

A. Allocation of Profits. Except as otherwise provided in Sections IX.3, IX.4, and IX.5 of this Agreement, Profits of the Company for each Fiscal Year shall be allocated to the Members as follows:

- 1) First, to 80% to Highland and 20% to Timberline until Parity is attained;
- 2) Second, to the Members, in proportion and to the extent of any Losses allocated to the Members pursuant to Section IX.1.B.4 below until each Member has been allocated an amount of cumulative Profits pursuant to this Section IX.1.A.2 in the current and all prior Fiscal Years equal to the cumulative Losses allocated to that Member pursuant to Section IX.1.B.4 below in all prior Fiscal Years;
- 3) Third, in proportion and to the extent of any Losses allocated to the Members pursuant to Section IX.1.B.3 below until each Member has been allocated an amount of cumulative Profits pursuant to this Section IX.1.A.3 in the current and all prior Fiscal Years equal to the cumulative Losses allocated to that Member pursuant to Section IX.1.B.3 below in all prior Fiscal Years;
- 4) Fourth, to the Members in accordance with their Percentage Interests.

B. Allocation of Losses. Except as otherwise provided in Sections IX.3, IX.4, and IX.5 of this Agreement, Losses of the Company for each Fiscal Year shall be allocated to the Members as follows:

- 1) First, 100.00% to Highland and 0.00% to Timberline until Parity is attained;

2) Second, to the Members, in proportion and to the extent of the Profits allocated to Members pursuant to Section IX.1.A.4 above, until each Member has been allocated an amount of cumulative Losses pursuant to this Section IX.1.B.2 in the current and all prior Fiscal Years equal to the cumulative Profits allocated to that Member pursuant to Section IX.1.A.4 above in all prior Fiscal Years;

3) Third, to the Members pro rata in accordance with their Percentage Interests, but with respect to a Member, only to the extent of the positive balance in such Member's Capital Account, until all Members' Capital Accounts have been reduced to zero; and

4) Fourth, to the Members pro rata in accordance with their Percentage Interests.

2. Allocations In General.

A. Except as otherwise provided herein, all items of Company income, gain, loss and deduction shall be divided among the Members in accordance with their Percentage Interests.

B. The Members are aware of the income tax consequences of the allocations made by this Section and hereby agree to be bound by the provisions of this Section in reporting their shares of Company income, gain, loss and deduction hereunder for income tax purposes.

C. For purposes of determining the Profits, Losses, or any other items allocable to any Fiscal Year, such items shall be determined on a daily, monthly, or other basis, as determined by the Management Committee, using any permissible method under Code Section 706 and the Regulations thereunder.

3. Tax Allocations Required by Code Section 704(c). In accordance with Code Section 704(c) and the Regulations thereunder, income, gain, loss and deduction with respect to any property contributed to the capital of the Company shall be allocated among the Members so as to take account of any variation between the adjusted basis of such property to the Company for federal income tax purposes and its initial Gross Asset Value.

If the Gross Asset Value of any Company property is adjusted pursuant to paragraph (b) of the definition of Gross Asset Value, subsequent allocations of income, gain, loss and deduction with respect to such property shall take account of any variation between the adjusted basis of such property and its Gross Asset Value in the manner provided under Code Section 704(c) and the Regulations thereunder.

Any elections or other decisions relating to such allocations shall be made by the Management Committee in any manner that reasonably reflects the purpose and intention of Code Section 704(c) and the Regulations thereunder.

4. Regulatory Allocations.

A. Minimum Gain Chargeback. Except as otherwise provided in Regulation Section 1.704-2(f) and notwithstanding any provision of this Section to the contrary (other than Section 4.B), if there is a net decrease in Company Minimum Gain during

any Fiscal Year, each Member shall be specially allocated items of Company income and gain for such Fiscal Year (and, if necessary, subsequent Fiscal Years) in an amount equal to such Member's share of the net decrease in Company Minimum Gain, determined in accordance with Regulation Section 1.704-2(g). Allocations pursuant to the previous sentence shall be made in proportion to the respective amounts required to be allocated to each Member pursuant thereto. The items to be so allocated shall be determined in accordance with Regulations Sections 1.704-2(f)(6) and 1.704-2(j)(2). This Section 4.A is intended to comply with the minimum gain chargeback requirement in Regulation Section 1.704-2(f) and shall be interpreted consistently therewith. For purposes of this Agreement, the term "Company Minimum Gain" shall have the meaning set forth in Regulation Section 1.704-2(b)(2), as if the word "Company" were substituted for the word "partnership" in such Regulation.

B. Member Minimum Gain Chargeback. Except as otherwise provided in Regulation Section 1.704-2(i)(4) and notwithstanding any provision in this Section to the contrary (other than Section 4.A), if there is a net decrease in Member Nonrecourse Debt Minimum Gain attributable to a Member Nonrecourse Debt during any Fiscal Year, each Member who has a share of the Member Nonrecourse Debt Minimum Gain attributable to such Member Nonrecourse Debt, determined in accordance with Regulation Section 1.704-2(i)(5), shall be specially allocated items of Company income and gain for such Fiscal Year (and, if necessary, subsequent Fiscal Years) in an amount equal to such Member's share of the net decrease in Member Nonrecourse Debt, determined in accordance with Regulation Section 1.704-2(i)(4). Allocations pursuant to the previous sentence shall be made in proportion to the respective amounts required to be allocated to each Member pursuant thereto. The items to be so allocated shall be determined in accordance with Regulation Sections 1.704-2(i)(4) and 1.704-2(j)(2). This Section 4.B is intended to comply with the partner minimum gain chargeback requirement in Regulation Section 1.704-2(i)(4) and shall be interpreted consistently therewith. For purposes of this Agreement, the term "Member Nonrecourse Debt" shall have the meaning set forth in Regulation Section 1.704-2(b)(2), and the term "Member Nonrecourse Debt Minimum Gain" shall have the meaning set forth in Regulation Section 1.704-2(i)(2), in each case as if the word "Member" were substituted for the word "partner" in such Regulations.

C. Qualified Income Offset. If any Member unexpectedly receives any adjustment, allocation or distribution described in Regulation Section 1.704-1(b)(2)(ii)(d)(4), (5) or (6), items of Company income and gain shall be specially allocated to such Member in an amount and manner sufficient to eliminate (to the extent required in the Regulations) any deficit in the Member's Capital Account created by such adjustment, allocation or distribution as quickly as possible; provided that, an allocation pursuant to this Section 4.C shall be made only if and to the extent that the Member would have a deficit in his or her Capital Account after all other allocations provided for in this Section 4 have been tentatively made as if this Section 4.C were not in the Agreement. This Section 4.C is intended to constitute a "qualified income offset" within the meaning of Regulation Section 1.704-1(b)(2)(ii)(d)(3).

D. Gross Income Allocation. In the event any Member has a deficit balance in such Member's Capital Account at the end of any Fiscal Year, which is in excess of the sum of the amount such Member is obligated to restore pursuant to the penultimate sentences of Regulation Sections 1.704-2(g)(1) and 1.704-2(i)(5), each such Member shall be specially allocated items of Company income and gain in the amount of such excess as quickly as possible; provided however, that an allocation pursuant to this

Section 4.D shall be made only if and to the extent that such Member would have such Capital Account deficit (as so determined) in excess of such sum after all other allocations provided for in this Section have been tentatively made as if Section 4.C and this Section 4.D were not in this Agreement.

E. **Nonrecourse Deductions.** Nonrecourse Deductions for any Fiscal Year shall be specially allocated to the Members in proportion to their Percentage Interests. For purposes of this Agreement, the term "Nonrecourse Deduction" shall have the meaning set forth in Regulation Section 1.704-2(b)(1).

F. **Member Nonrecourse Deductions.** Any Member Nonrecourse Deductions for any Fiscal Year shall be specially allocated to the Member who bears the economic risk of loss with respect to the Member Nonrecourse Debt to which such Member Nonrecourse Deductions are attributable in accordance with Regulation Section 1.704-2(i)(1). For purposes of this Agreement, the term "Member Nonrecourse Deductions" shall have the meaning set forth in Regulation Section 1.704-2(i)(1), as if the word "Member" were substituted for the word "partner" in such Regulation.

G. **Loss Allocation Limitation.** Losses allocated pursuant to this Section shall not exceed the maximum amount of Losses that can be allocated without causing any Member to have a deficit in his or her Capital Account at the end of any Fiscal Year. In the event some but not all of the Members would have a deficit in their Capital Accounts as a consequence of an allocation of Losses under this Section, the limitation set forth in this Section 4.G shall be applied on a Member by Member basis and Losses not allocable to any Member as a result of such limitation shall be allocated to the other Members in accordance with the positive balances in such Members' Capital Accounts so as to allocate the maximum permissible Losses to each Member under Regulation Section 1.704-1(b)(2)(ii)(d).

H. **Section 754 Adjustments.** To the extent an adjustment to the adjusted tax basis of any Company property is required, pursuant to Code Sections 734(b) or 743(b) or Regulations Sections 1.704-1(b)(2)(iv)(m)(2) or 1.704-1(b)(2)(iv)(m)(4), to be taken into account in determining the Capital Accounts as the result of a distribution to a Member in complete liquidation of such Member's Interest in the Company, the amount of such adjustment to the Capital Accounts shall be treated as an item of gain (if the adjustment increases the basis of the property) or an item of loss (if the adjustment decreases the basis of the property) and such gain or loss shall be specially allocated to the Members in accordance with their Percentage Interests in the Company in the event Regulation Section 1.704-1(b)(2)(iv)(m)(2) applies, or to the Member to whom such distribution was made in the event Regulation Section 1.704-1(b)(2)(iv)(m)(4) applies.

5. **Curative Allocations.** The allocations set forth in Section 4 (the "Regulatory Allocations") are intended to comply with the requirements of Code Section 704(b) and the Regulations thereunder. It is the intent of the Members that, to the extent possible, all Regulatory Allocations shall be offset either with other Regulatory Allocations or with special allocations of other items of Company income, gain, loss or deduction pursuant to this Section 5. Therefore, notwithstanding any other provision of this Section (other than the Regulatory Allocations), the Management Committee shall make such offsetting special allocations of Company income, gain, loss or deduction in whatever manner the Management Committee determines appropriate so that, after such offsetting allocations are made, each Member's Capital Account balance is, to the extent possible, equal to the Capital Account balance such

Member would have had if the Regulatory Allocations were not part of the Agreement and all Company items were allocated pursuant to Sections 1, 2 and 3.

6. **Distributions.** Distributions shall be made to the Members on a quarterly basis, as follows, unless such Distributions are prohibited by the Code, the Regulations or by any other law or court decree:

A. Until Parity is reached, all Distributions shall be made in the ratio of 80% to Highland and 20% to Timberline (for the avoidance of doubt, Distributions shall include the repayment of the Loan to the Company by Highland pursuant to the Loan Documents);

B. When Parity is reached, Distributions shall be made in the ratio of 100% to Highland and 0% to Timberline until the Capital Accounts of the Members are equal;

C. After Parity is reached and Capital Accounts are equalized in Section 6.B, above, then to the Members in accordance with their Percentage Interests.

7. **Consent to Allocations and Distributions.** The methods set forth in this Section by which allocations and Distributions are made is expressly consented to by each Member as a condition of becoming a Member. Attached as Exhibit D is a schedule showing the intent of the allocations and distributions described in this Agreement.

8. **Distribution Among Members.** If a transfer of an Interest in the Company occurs during any accounting period as permitted hereunder, all Profits, Losses and other items attributable to such Interest for such period shall be divided and allocated between the transferor and the transferee by taking into account their varying interests during the period in accordance with Code Section 706(d), using any conventions permitted by law and selected by the Management Committee. All allocations and Distributions on or before the date of a permitted transfer shall be made to the transferor, and all allocations and Distributions thereafter shall be made to the transferee. Solely for purposes of making such allocations and Distributions, the Company shall recognize a permitted transfer not later than the end of the calendar month during which the transfer is effective, pursuant to Section X of this Agreement. Neither the Members, the Representatives nor the Company shall incur liability for making allocations and Distributions in accordance with the provisions of this Section 8, whether or not the Members, the Representatives or the Company have knowledge of any transfer of ownership of any Interest in the Company.

9. **Amounts Withheld.** All amounts withheld, pursuant to the Code or any provision of any federal, state or local tax law, with respect to any payment or Distribution to the Members shall be treated as amounts distributed to the Members pursuant to this Section for all purposes under this Agreement.

10. **Special Basis Adjustment.** In connection with any transfer of an Interest in the Company as permitted hereunder, the Management Committee may cause the Company, at the written request of the transferor or the transferee or if required by law, and at the time and in the manner provided in Regulation Section 1.754-1(b) and Code Sections 734(b) or 743(b), to make an election to adjust the basis of the Company's property in the manner provided in Code Sections 734(b) and 743(b) and any Regulations thereunder, and if such election is made, such transferee shall pay all costs and expenses incurred by the Company in connection therewith, including, without limitation, reasonable attorneys' and accountants' fees.

11. **Taxable as a Partnership.** Unless all of the Members otherwise agree in writing, the Company shall not elect to be treated as an association, taxable as a corporation, for federal or state income tax purposes; the Company shall be treated as a partnership for federal and state income tax purposes.

X. **TRANSFERABILITY OF INTERESTS.**

1. **No Transfer.** Neither the Company, the Management Committee nor the Members shall permit or recognize any sale, redemption, assignment, gift, bequest, pledge or other transfer, whether by operation of law or otherwise (collectively, "Transfer") of any Interest except in accordance with the provisions of this Section X and Section XIII.

2. **No Withdrawal.** No Member shall have the right or power to withdraw his or her share of the Company capital or compel a redemption of his or her Interests by the Company.

3. **Substituted Member.** Notwithstanding an otherwise valid transfer of an Interest, the transferee shall not become a Member and the transferring Member shall not be relieved of any of its obligations until the transferee has:

A. Accepted and assumed, in a form reasonably satisfactory to the non-transferring Member, all of the terms and provisions of this Agreement;

B. Executed such other documents or instruments as the non-transferring Member may reasonably require in order to effect the admission of the transferee as a Member; and

C. Paid such reasonable expenses as may be incurred by the Company in connection with the admission of the transferee.

4. **Effective Date.** The effective date of a Transfer of Interests shall be the last day of the calendar month in which such transfer occurs.

5. **Rights of Substituted Member.** After the effective date of a Transfer of Interests, a Substituted Member (admitted pursuant to Section X hereof) shall have all the rights of the Member from whom the Substituted Member received such Interest.

XI. **METHOD OF ACCOUNTING, RECORDS AND REPORTS.**

1. **Method of Accounting.** The Controller shall maintain the books, records and accounts of the Company in accordance with Generally Accepted Accounting Principles (GAAP), and shall report income for tax and income tax purposes, in each case consistent with Highland's accounting practices and as required by the reporting requirements of any Member. The Company's financial records shall be maintained at the Company's principal business office. Each Member shall have the right upon reasonable notice given to the other to inspect, extract and copy the Company's books and records.

2. **Unaudited Financial Reports.** The Controller shall provide combined quarterly unaudited income statements, balance sheets and statements of cash flow to the Management Committee relating to the Company operations with such content as the Management Committee shall direct on a regular and timely basis. Such quarterly financial statements shall cover each calendar month and be delivered within twenty-five (25) days following the end of each month.

3. **Tax Returns and Reports.** The Controller, with the assistance of the tax matters partner, shall cause the preparation and timely filing of all required federal and state tax returns and other reports for the Company each year. The Controller shall deliver copies of the Company's tax returns for each Fiscal Year to the Members by April 15th of the following Fiscal Year. The Controller shall deliver copies of each of the Company's other reports, if any, to the Management Committee within ten (10) days before the due date of the applicable report.

4. **Fiscal Year.** The Company shall adopt the calendar year for tax and financial reporting purposes (the "Fiscal Year").

XII. **TERMINATION AND DISSOLUTION OF THE COMPANY.**

1. **Termination.** Subject to Section XIII, the Company shall be terminated and dissolved upon the occurrence of the following:

A. The unanimous written consent of all the Members to the termination and dissolution of the Company;

B. The default by a Member to fulfill in any material respect any of its obligations under this Agreement (unless waived by the other Member);

C. The default by the Company to fulfill in any material respect any of its obligations under this Agreement; or

D. Upon the happening of any events ("Dissolution Events") listed in the Act (membership termination by dissolution) unless the business of the Company is continued pursuant to a majority vote of the remaining Member(s).

2. **Actions Following Termination.** Upon the occurrence of any event causing the termination and dissolution of the Company, the Members shall take full account of the Company's property and liabilities, and endeavor to liquidate the property promptly while maximizing the proceeds realizable therefrom. The proceeds realized from disposition of property shall be applied and distributed in the following order and within the following time periods:

A. To the payment of creditors of the Company, including affiliates or parties related to a Member, other than Members in the order of priority as provided by law, excluding creditors whose obligations will be assumed or otherwise transferred on liquidation of the Company;

B. To the payment of creditors of the Company who are Members;

C. To the setting up of reserves which the Members, by a unanimous vote, deem reasonably necessary for liabilities not then due and contingent liabilities of the Company;

D. To the Members in accordance with their positive Capital Accounts (after giving effect to all contributions, distributions and allocations for all periods, including taking into account all Capital Account adjustments for the Company's taxable year during which the liquidation occurs, by the end of such taxable year, or if later, within ninety (90) days after the date of such liquidation);

E. To the Members in accordance with their share of Distributions pursuant to Section IX of this Agreement.

3. **Notice, Mitigation and Cure.** An event of termination under Section 1.A shall not arise until and unless (a) the non-defaulting Member shall have given written notice to the defaulting Member of the facts constituting such breach or failure, and (b) unless such defaulting Member shall have failed, within thirty (30) days following receipt of such notice, to have cured, remedied or mitigated such breach or failure to the satisfaction of the non-defaulting Member.

4. **No Election of Remedies.** No action taken by a Member pursuant to this Agreement shall constitute an election of remedies, and such Member may pursue rights and remedies it may have at law or in equity.

5. **Deficit Capital Accounts.** Notwithstanding anything to the contrary contained in this Agreement, and notwithstanding any custom or rule of law to the contrary, upon dissolution of the Company, a deficit in a Member's Capital Accounting shall not be an asset of the Company and such Member shall not be obligated to contribute such amount to the Company to bring the balance of such Member's Capital Account to zero.

XIII. **DEFAULT OPTIONS AND CHANGE OF CONTROL.**

1. **Highland Default Option.** In the event of a default by Highland (or its Affiliate) as described in Sections XII.1.B or XII.1.C that remains uncured, a Dissolution Event with respect to Highland, or a default by the Company which may be waived by Timberline under Section XII.1.C., Timberline may elect to exercise the provisions of Section XIII.4. below.

2. **Timberline Default Option.** In the event of a default by Timberline (or its Affiliate) as described in Sections XII.1.B. or XII.1.C. that remains uncured, a Dissolution Event with respect to Timberline, or a default by the Company which may be waived by Highland under Section XII.1.C., Highland may elect to exercise the provisions of Section XIII.4. below.

3. **Deadlock Options.** In the event of a Deadlock that commences on or after the Parity is reached, either party may elect to exercise the provisions of Section XIII.4. below.

4. **Buy - Sell Election.** If there is an election under Sections XIII. 1, 2, or 3 above to exercise the provisions of this Section 4, then the electing Member shall have the option to determine the price at which the electing Member will sell its entire Interest to the non electing Member, and at which it is willing to purchase the entire Interest of the non electing Member. The electing Member shall give such a notice (an "Option Notice") to the non electing Member of this price. The non electing Member shall have thirty (30) days to respond in writing to the electing Member (a "Response Notice"). The Response Notice shall indicate whether the non electing Member desires to purchase the Interest of the electing Member, or sell its Interest to the electing Member, at the price the electing Member provided in its Option Notice. The Members shall thereafter cooperate to close the purchase and sale of the Interest to be sold. Closing of the purchase and sale of the Interest to be sold shall be not later than one hundred and twenty (120) days after the date of the Response Notice.

5. **Change of Control.** If a Change of Control occurs with respect to a Member, then the other Member shall have the option of adding one additional voting representative to the Management Committee. Such representative may be added within thirty (30) days following the day of the Change of Control.

6. **Option Notice Requirements.** If a party elects to exercise any of its options pursuant to this Section XIII, such party shall deliver a Option Notice to the other Member. The Option Notice shall identify the option being exercised and the Member's proposed purchase price for its or the other Member's Interest, or in the case of a Change of Control, the notice shall provide that the electing Member is exercising its option to add a representative to the Management Committee, and the name and address of the additional representative. The closing of the purchase and sale of an Interest pursuant to this Section XIII shall take place as follows: (i) the purchase price shall be payable in cash at closing, (ii) the Interest shall be conveyed free and clear of all liens, claims and encumbrances.

XIV. **INDEMNIFICATION; REIMBURSEMENT**

1. **Indemnification.** Each Member hereby indemnifies defends and holds harmless and agrees to defend the other Members and the Company from and against any and all claims, losses, damages, demands, liabilities, obligations, penalties, actions or rights of action, judgments, suits, costs, expenses, or disbursements of any kind or nature which may arise as a result of any:

A. Breach of this Agreement by the indemnifying Member; or

B. Action by the indemnifying Member or any of its officers, directors, employees, or agents with respect to the Company, which action has not been authorized pursuant to the terms of this Agreement.

2. **Notice of Claims.** Any party entitled to indemnification ("Indemnified Party") agrees to give the indemnifying party (the "Indemnitor") notice of any and all claims asserted against the Indemnified Party for which indemnification is or may be sought under this Section XIV. Such notice shall be given within a reasonable time after receipt of written notice of such claim by the Indemnified Party. Failure to give such notice shall not abrogate or diminish the Indemnitor's obligation under this Section XIV if the Indemnitor has or receives knowledge of the existence of any such claim by any other means or if such failure does not prejudice the Indemnitor's ability to defend such claim.

3. **Defense of Claim.** In any litigation, administrative proceeding, negotiation or arbitration pertaining to any claim for which indemnification is sought under this Section XIV, the Indemnitor shall have the right to select legal counsel to represent the Indemnitor and to otherwise control such litigation, proceedings, negotiations and arbitration. If the Indemnitor elects to control such litigation, proceeding, negotiation or arbitration, the Indemnified Party shall at all times have the right to fully participate in the defense at its own expense. If the Indemnitor shall, within a reasonable time after notice, fail to defend, the Indemnified Party shall have the right, but not the obligation, to undertake the defense of and to compromise or settle the claim or other matter on behalf of, for the account of, and at the risk of, the Indemnitor.

4. **Reimbursement.** The Company shall reimburse Members for any amounts which, pursuant to approval by the Representatives or final judgment of any court of applicable jurisdiction, have been paid by such Member on behalf of or for the account of the Company with respect to: (i) any liability, obligation, undertaking, damage, or claim for which the Company shall or may, pursuant to contract or applicable law, be liable or responsible, or (ii) making good any loss or damage sustained by, or paying any duty, cost, claim, or damage incurred by the Company. If the Company fails to fully reimburse a Member that made such payment, then the other Members shall pay a proportionate amount, based on the Interests

held by such Member, of the amount still unpaid to the Member that made the original payment. This final payment shall be made within thirty (30) days of the date the reimbursement was requested from the Company

5. **Relationship.** Without the prior written consent of the Members or unless otherwise stated herein, no Member shall have the power or authority to act for or on behalf of the other or for the account of the Company. Each Member will look solely to the assets of the Company for the return of its respective capital, and if the assets remaining after payment or discharge, or provision for payment or discharge, of the Company's debts or liabilities are insufficient to return the capital to the Members, no Member will have any recourse against the separate assets of the other Member for that purpose; provided, however, that this provision will in no way limit the indemnification provisions contained in this Section.

XV. **DEFINITION OF TERMS.**

1. **"Act"** means the Idaho Limited Liability Company Act, as amended from time to time, or the provisions of any successor legislation.

2. **"Agreement"** means this Operating Agreement as originally executed and as amended from time to time.

3. **"Affiliate"** means a Person that directly, or indirectly through one or more intermediaries, owns or controls, is owned or is controlled by, or is under common ownership or control with a Member. As used herein, "control" means the power to direct the management or affairs of a Member or other Person, and "ownership" means the beneficial ownership of more than fifty percent (50%) of the equity securities of the Member or other Person.

4. **"Ancillary Agreements"** means the Agreement, the SMD Agreement, and the Loan Documents.

5. **"Capital Account"** means, with respect to any Member, a capital account maintained for such Member on the books of the Company in accordance with the following provisions:

A. To each Member's Capital Account there shall be credited (i) such Member's Capital Contributions, (ii) such Member's distributive share of the Profits and any items in the nature of income or gain which may be specially allocated to such Member pursuant to Section IX hereof, and (iii) the amount of any Company liabilities assumed by such Member or which are secured by any property distributed to such Member;

B. To each Member's Capital Account there shall be debited (i) the amount of cash and the Gross Asset Value of any property distributed to such Member pursuant to any provision of this Agreement, (ii) such Member's distributive share of the Losses and any items in the nature of expenses or losses which are specially allocated to such Member pursuant to Section IX hereof, and (iii) the amount of any liabilities of such Member assumed by the Company or which are secured by any property contributed by such Member to the Company; and

C. In the event any Interest in the Company is transferred in accordance with the terms of this Agreement, the transferee shall succeed to the Capital Account of the transferor to the extent the Capital Account relates to the transferred Interest.

The foregoing provisions and the other provisions of this Agreement relating to the maintenance of Capital Accounts are intended to comply with Regulation Section 1.704-1(b), and the Capital Accounts of the Members shall be maintained in a manner consistent with such Regulation. In the event the Management Committee shall determine that it is prudent to modify the manner in which the Capital Accounts, or any debits or credits thereto are computed in order to comply with such Regulation, the Management Committee may make such modification; provided that, it is not likely to have a material effect on the amounts distributable to any Member pursuant to Section XII hereof upon the dissolution of the Company. The Members also shall: (a) make any adjustments that are necessary or appropriate to maintain equality between the Capital Accounts of the Members and the amount of Company capital reflected on the Company's balance sheet, as computed for book purposes in accordance with Regulation Section 1.704-1(b)(2)(iv)(q); and, (b) make any appropriate modifications in the event unanticipated events might otherwise cause this Agreement not to comply with Regulation Section 1.704-1(b).

6. "Capital Contributions" means, with respect to any Member, the amount of cash and the initial Gross Asset Value of any property (other than cash) contributed to the Company with respect to the Company Interest held by such Member pursuant to the terms of this Agreement. Such property shall include but not be limited to property received by the Company pursuant to a merger, exchange or similar transaction in which a Person transfers property to the Company in return for an Interest in the Company. The principal amount of a promissory note which is not readily traded on an established securities market and which is contributed to the Company by the maker of the promissory note shall not be included in the Capital Contribution of any Person until the Company makes a taxable disposition of the promissory note or until (and only to the extent) principal payments are made on the promissory note, all in accordance with Regulation Section 1.704-1(b)(2)(iv)(d)(2).

7. "Change of Control" means with (i) respect to Highland, an event after which causes the family of Ron Guill (including his spouse, children and children of his children to own less than 50% of the membership interests of Highland and (ii) with respect to Timberline, if there is a change of more than 50% of the members of the board of directors of Timberline in any twelve (12) month period.

8. "Code" means the Internal Revenue Code of 1986, as amended from time to time (and any comparable or successor provisions to the Code sections referenced in this Agreement).

9. "Company" means the Company existing under the terms of this Agreement.

10. "Deadlock" means the failure of the Representatives appointed by each Member to agree on a major action enumerated in Section V.8 following (i) two (2) meetings in which such action has been discussed and a vote taken, and (ii) following a mediation of the action at which the Members cannot agree with respect to the major action. If there is a failure to agree on such a major action following two (2) such meetings, then the Members shall submit the major action to non-binding mediation within thirty (30) days following the second meeting. The mediator selected shall be acceptable to both Members. The Members shall act in good faith and reasonably cooperate with each other and with the mediator. The mediation shall be completed within ninety (90) days following the date the major action is submitted to mediation.

The results of the mediation shall not be binding upon the Members. The mediation shall occur at the principal place of business of the Company. If the mediation is not completed within such ninety (90) day period, then there shall be a Deadlock.

11. "Depreciation" means, for each Fiscal Year or other period, an amount equal to the depreciation, amortization, or other cost recovery deduction allowable with respect to an asset for such Fiscal Year or other period, except that if the Gross Asset Value of an asset differs from its adjusted basis for federal income tax purposes at the beginning of such Fiscal Year or other period, Depreciation shall be an amount which bears the same ratio to such beginning Gross Asset Value as the federal income tax depreciation, amortization, or other cost recovery deduction for such Fiscal Year or other period bears to such beginning adjusted tax basis; provided however, that if the federal income tax depreciation, amortization, or other cost recovery deduction for such Fiscal Year is zero, Depreciation shall be determined with reference to such beginning Gross Asset Value using any reasonable method selected by the Members.

12. "Distributable Cash" means the Company cash and cash equivalents on hand less cash required for operations of the Company and reasonable reserves for contingencies and anticipated obligations, all as determined by the Management Committee. The Members agree that there shall be no Distributable Cash until the Company has retained working capital of not less than Five Million Dollars (\$5,000,000).

13. "Distribution" means property, cash or Distributable Cash distributed to Members because of their status as Members, or as a lender to the Company.

14. "Gross Asset Value" means, with respect to any property, the property's adjusted basis for federal income tax purposes, except as follows:

A. The initial Gross Asset Value of any property contributed by a Member (including a former Member) to the Company shall be the gross fair market value of such property, as determined by the Members;

B. The Gross Asset Values of all Company property shall be adjusted to equal their respective gross fair market values as determined by the Members, as of the following times: (i) the acquisition of an additional Interest in the Company by any new or existing Member in exchange for more than a de minimis Capital Contribution; (ii) the Distribution by the Company to a Member of more than a de minimis amount of property as consideration for an Interest in the Company; and (iii) the liquidation of the Company within the meaning of Regulation Section 1.704-1(b)(2)(ii)(g); provided however, that adjustments pursuant to clauses (i) and (ii) above shall be made only if the Members reasonably determine that such adjustments are necessary or appropriate to reflect the relative economic interests of the Members in the Company;

C. The Gross Asset Value of any Company property (other than cash) distributed to any Member shall be the gross fair market value of such property on the date of Distribution; and

D. The Gross Asset Value of Company property shall be increased (or decreased) to reflect any adjustments to the adjusted basis of such assets pursuant to Code Section 734(b) or Code Section 743(b) but only to the extent that such adjustments are taken into account in determining the Members' Capital Accounts pursuant to either Regulation Section 1.704-1(b)(2)(iv)(m) or Code § 743(b) in the case of a substantial

built-in loss; provided however, that Gross Asset Values shall not be adjusted pursuant to this paragraph to the extent the Members determine that an adjustment pursuant to paragraph (b) above is necessary or appropriate in connection with a transaction that would otherwise result in an adjustment pursuant to this paragraph (d).

E. If the Gross Asset Value of any property has been determined or adjusted pursuant to this definition, such Gross Asset Value shall thereafter be adjusted by the Depreciation taken into account with respect to such property for purposes of computing Profits and/or Losses.

15. "Interest" when used alone without reference to specific type of Interest, a Member's Percentage Interest in the Company, represented by the Member's Capital Account, the right to share in Distributions and the right to vote as a Member and participate in the Company's management to the extent provided in this Agreement.

16. "Loan" means the loan from Highland to the Company evidenced by the Loan Documents. If the Loan is not called or terminated early, for any reason, and the loan is being repaid by the Company, then, when the balance of the Loan is \$2,000,000, the Loan shall be converted from loan to a Capital Contribution.

17. "Loan Documents" means the loan agreement, promissory note and other agreements and/or documents substantially in the form attached hereto as Exhibit C evidencing the loan from Highland to the Company.

18. "Management Committee" means the person or entity serving as Management Committee pursuant to Section V of this Agreement.

19. "Member" means each of the parties who executes a counterpart of this Agreement, or may hereafter be admitted, as a member of the Company in compliance with the terms of this Agreement (including a Substituted Member after being admitted pursuant to Section X.3).

20. "Parity" means the date at which the investment by Timberline is deemed equal to the investment by Highland. This shall not occur until the Loan from Highland, including all principal, interest and other related amounts, is repaid, except for principal in the amount of Two Million Dollars (\$2,000,000.00).

21. "Percentage Interest" means, with respect to any Member, the percentage determined by dividing the amount of such Member's Capital Account by the sum of all Members' Capital Accounts. The sum of all Members' Percentage Interests shall equal one hundred percent (100%). The Percentage Interests shall be set forth in Exhibit "A".

22. "Person" means any natural person, partnership (general or limited), corporation, association, limited liability company, trust, estate or other legal entity.

23. "Profits" and/or "Losses" means, for each Fiscal Year or other period, an amount equal to the Company's taxable income or loss for such Fiscal Year or period, determined in accordance with Code Section 703(a) (for this purpose, all items of income, gain, loss, or deduction required to be stated separately pursuant to Code Section 703(a)(1) shall be included in taxable income or loss), with the following adjustments (without duplication):

A. Any income of the Company that is exempt from federal income tax and not otherwise taken into account in computing Profits and/or Losses pursuant to this definition shall be added to such taxable income or loss;

B. Any expenditures of the Company described in Code Section 705(a)(2)(B) (relating to Company expenditures not deductible in computing taxable income and not properly chargeable to a capital account) or treated as Code Section 705(a)(2)(B) expenditures pursuant to Regulation Section 1.704-1(b)(2)(iv)(i), and not otherwise taken into account in computing Profits and/or Losses pursuant to this definition, shall be subtracted from such taxable income or loss;

C. If the Gross Asset Value of any Company property is adjusted pursuant to paragraph (b) or (d) of the definition of Gross Asset Value, the amount of such adjustment shall be taken into account as an item of gain (if the adjustment increases the Gross Asset Value) or an item of loss (if the adjustment decreases the Gross Asset Value) from the disposition of such property for purposes of computing Profits and/or Losses;

D. Gain or loss resulting from any disposition of property with respect to which gain or loss is recognized for federal income tax purposes shall be computed by reference to the Gross Asset Value of the property disposed of, notwithstanding that the adjusted tax basis of such property differs from its Gross Asset Value; and

E. In lieu of the depreciation, amortization, and other cost recovery deductions taken into account in computing such taxable income or loss, there shall be taken into account Depreciation for such Fiscal Year or other period, computed in accordance with the provisions hereof.

24. "Regulation" means the income tax regulation promulgated under the Code, as such regulation may be amended from time to time (and any comparable or successor provisions to the Regulation sections referenced in this Agreement).

25. "SMD Agreement" means the Agreement dated _____, 2009, between the Company and Small Mine Development, LLC, an Idaho limited liability company, for the development of the Property.

26. "Substituted Member" means a transferee of a Member's Interest who has succeeded as a Member to all of the rights inherent in the ownership of his or her Interest and as to whom all of the requirements of Section X have been satisfied.

XVI. MISCELLANEOUS.

1. Counterparts. This Agreement may be executed in several counterparts, and all copies so executed shall constitute one agreement, binding on all of the parties hereto, notwithstanding that all the parties are not signatories to the original or the same counterpart.

2. Notices. Unless otherwise provided, all notices under this Agreement shall be in writing and shall be given to the Person entitled thereto, by (i) personal delivery, (ii) U.S. registered or certified mail, or (iii) delivery via reputable overnight courier, to the address indicated in the Company's records for such Person. If mailed, such notice shall be deemed to be delivered two (2) business days after being deposited in U.S. mail, with postage prepaid, to the applicable Person's address set forth on Exhibit "A".

3. **Application of Idaho Law.** This Agreement, and the application and interpretation hereof, shall be governed exclusively by its terms and by the laws of the State of Idaho and specifically the Act.
4. **Waiver of Action for Partition.** During the term of the Company, each Member irrevocably waives any right that such Member may have to maintain any action for partition with respect to the property of the Company. The Members intend that the Company is a limited liability company. The Members are not partners or joint venturers for any purposes other than federal and state income tax purposes, and this Agreement shall not be construed to provide otherwise.
5. **Construction.** Whenever a singular term is used in this Agreement, such term shall also include the plural version of the term when the context requires. Whenever a masculine term is used in this Agreement, such term shall also include the feminine and neutral versions of the term when the context requires.
6. **Headings.** The headings in this Agreement are inserted for convenience only and are in no way intended to describe, interpret, define, or limit the scope, extent or intent of this Agreement or any provision hereof.
7. **Waivers.** The failure of any party to seek redress for violation of, or to insist upon the strict performance of, any covenant or condition of this Agreement shall not prevent a party from seeking redress or insisting on strict performance for any subsequent violations of this Agreement by another party.
8. **Rights and Remedies Cumulative.** The rights and remedies provided by this Agreement are cumulative and the use of any one right or remedy by any party shall not preclude or waive the right of any party to use any or all other remedies available to a party under the law. The rights and remedies given to a party under this Agreement are given in addition to any other rights a party may have by law, statute, ordinance or otherwise.
9. **Severability.** If any provision of this Agreement or the application thereof to any Person or circumstance shall be invalid, illegal or unenforceable to any extent, the remainder of this Agreement and the application thereof shall not be affected and shall be enforceable to the fullest extent permitted by law.
10. **Binding Effect.** Each and all of the covenants, terms, provisions and agreements herein contained shall be binding upon and inure to the benefit of the parties hereto and their respective heirs, legal representatives, successors, assigns, owners, employees, agents, directors, officers and Management Committees, as applicable.

IN WITNESS WHEREOF, the Company and the Members hereby execute this Agreement effective as of the 22 day of July, 2009.

COMPANY:

BUTTE HIGHLANDS JV, LLC

By: Ronald W. Giff

Its: MANAGER

MEMBERS:

TIMBERLINE RESOURCES CORPORATION

By: Ronald L. Hardy

Its: CEO

HIGHLAND MINING, LLC

By: Ronald W. Giff

Its: MANAGER

EXHIBIT "A"

THE SCHEDULE

Name	U.S. Mail Address Phone Number Email Address (as applicable)	Percentage Interest
Timberline Resources Corporation	101 E. Lakeside Avenue Coeur d'Alene, ID 83814 Attn: Randal Hardy (208) 664-4859 Phone (208) 664-4860 Fax hardy@timberline-resources.com	50%
Highland Mining, LLC	967 East ParkCenter Blvd. PMB 174 Boise, ID 83702 Attn: Ron Guill (208) 338-8880 Phone (208) 338-8881 Fax rquill@undergroundmining.com	50%
TOTAL		100%

EXHIBIT "B"

SMD AGREEMENT

SMALL MINE DEVELOPMENT, LLC

907 E. PARKCENTER BLVD. PMB #396
BOISE, IDAHO 83708-6700
PH: 208-338-8880
FX: 208-338-8881

6/25/2009

TO: General Manager
Butte Highlands LLC - JV
FROM: SMD-LLC
SUBJ: Butte Highlands JV Exploration Project

GENERAL SCOPE OF WORK - EXHIBIT A

- 1) Mobilization and surface site preparations
- 2) Establishment of Portal
- 3) Drive approximately 6,700' of drift/amp/ventilation raise/bulk sample
- 4) Demobilization

PROPOSED RATES

	type work	size	unit price	unit	#units	notes	total price
1)	Mobilization		\$ 85,000.00	1 s.	1		85,000.00
2)	Surface excavations/preparations/ponds/linings (by others)		\$ 1,000,000.00	1 s.	1	estimate	1,000,000.00
3)	Surface setups including concrete/structure install/piping/etc					estimate	150,000.00
4)	Portal w/25'	16' X 14'				estimate	100,000.00
5)	Drifting - single heading	16' X 14'				estimate	7,250,000.00
6)	Drifting - multiple heading	16' X 14'				estimate	705,000.00
7)	Drifting - ore development for bulk sample	16' X 14'				estimate	587,500.00
8)	Ventilation raise (boored by others or allinac)	10' x 10'				estimate	720,000.00
9)	Shotcrete material + application	> 1"				estimate	180,000.00
10)	8' resin bolts + intersections & as required	8"				estimate	24,000.00
11)	Demobilization		\$ 85,000.00	1 s.	1		85,000.00
							10,299,000.00

NOTES:

- A) #1 - includes equipment freight + labor to site
- B) #2 - all surface excavations including portal cut, roads, ponds, ditching, linings, compacting, etc. (work to be subcontracted)
- C) #3 - includes all work required to get surface site setup and ready to start portal work after earth work is completed
- D) #4 - includes highwall preparations with bolts/wire/shotcrete + use of SMD trackhoe w/cutterhead for establishment of collar
- E) #4 - not expected to use steel @ portal
- F) #5, #6, #7 - all rates for drifting @ 16' X 14' and boored utilizing 6' splitsels + 4"X4" welded wire panels + shotcrete as required on ribs
- G) #5, #6, #7 - all drifts larger than 16' X 14' (224 ft2) will be based on equivalent footage (Area/224)
- H) #8 - geotech hole required to determine which method will be used (exact price will vary and may be completed by subcontractor)
- I) #9 - shotcrete application to include equipment + labor + shotcrete materials
- J) #10 - rate for bolt installation as needed @ intersections
- K) #11 - includes equipment freight + site cleanup

SMD PERSONNEL

- 1) Project superintendent
- 2) U/G mechanic
- 3) U/G miners

4
5
10-20

EXHIBIT A B

REDACTED*

REDACTED #

PROPOSED WORK SCHEDULE

- 1) 2-12 hr. shift/day
- 2) 7 on - 7 off schedule

SMD SUPPLIED EQUIPMENT (as may be required)

- | | |
|-------------------------------|---|
| 1) 6 yd3 LHD | 2 |
| 2) Tamrock twin boom jumbo | 1 |
| 3) Tamrock boiler | 1 |
| 4) Tamrock EJC-522 truck | 1 |
| 5) Wet shotcrete setup | 2 |
| 6) German AG4 ET | 1 |
| 7) German AG4 SD | 1 |
| 8) 8042 skyrac | 1 |
| 9) Elmac DA100A water truck | 2 |
| 10) R100 u/g grader | 1 |
| 11) IR 825 diesel compressor | 1 |
| 12) Cat 545 kw genset | 1 |
| 13) Cat 320 kw genset | 1 |
| 14) U/G tractor | 1 |
| 15) Cat IT-28F surface loader | 2 |
| 16) Pickup | 1 |

SMD SUPPLIED MATERIALS (all general drilling + maintenance supplies including.)

- 1) Explosives
- 2) Diesel fuel/oil
- 3) Ground support materials (steelbolts/nails/wire/shotcrete/etc.)
- 4) Piping materials
- 5) 48" ventilation ducting + booster fans
- 6) All 13800V electrical distribution
- 7) All u/g electrical to 480V

NOTES:

- A) none

OWNER SUPPLIED MATERIALS/EQUIPMENT

- 1) Office
- 2) Dry/change room
- 3) Escape holel (if necessary)
- 4) Shop tent
- 5) Water tanks/drip system
- 6) Fuel tanks

NOTES:

- A) none

OTHER OWNER RESPONSIBILITIES/SUPPORT REQUIRED

- 1) Request and maintain all required federal/state/country permits
- 2) Provide site specific MSHA training for SMD personnel
- 3) Provide drill water as required

EXHIBIT A/5

- 4) Provide use of Phone/fax as needed

OTHER SMD RESPONSIBILITIES

- 1) Provide owner with proof of insurances as appropriate
- 2) Provide all required MSHA training/records for SMD site personnel
- 3) Provide engineering/geologic controls as required

GENERAL PARAMETERS

- 1) It is assumed that this work will encounter no significant ground water inflow (>50 gpm)

PAYMENT TERMS

- 1) Due as earned, invoicing at the end of each month - payable to SMD by the 15th of the next mo.

After you have had a chance to review this information, please give me a call at 208-338-8880 so that I can answer any questions/concerns that you might have with any of the above numbers


Sincerely,
Ronald W. Gull
Owner-Mgr/SMD

EXHIBIT A B

EXHIBIT "C"

LOAN DOCUMENTS

PROMISSORY NOTE

Maker: Butte Highlands JV, LLC

Holder: Highland Mining, LLC

Date of Making: July 22, 2009

Place of Making: Boise, Idaho

Principal Amount: Amount of Advances plus other amounts

Interest Rate: Four percent (4.0%) per annum, compounded continuously

Maturity Date: Upon demand (the "Maturity Date")

FOR VALUE RECEIVED, the undersigned, Butte Highlands JV, LLC, an Idaho limited liability company, whose address is 967 East ParkCenter Boulevard, Boise, Idaho 83716 ("Maker"), promises to pay to Highland Mining, LLC, an Idaho limited liability company, whose address is 967 East ParkCenter Boulevard, Boise, Idaho 83716 ("Holder"), at 967 East ParkCenter Boulevard, Boise, Idaho 83716, or such other place as may be designated from time to time in writing by the holder of this Note, the amounts advanced under this Note in the sole discretion of Holder, in lawful money of the United States of America, plus interest thereon at the rate set forth herein until paid in full. Interest shall be calculated on the basis of a 365 day year.

1. Interest Rates. Interest shall accrue on the unpaid principal balance of this Note at the rate of four percent (4.0%) per annum from July 22, 2009, until paid in full upon the demand of the Holder (the "Maturity Date").
2. Payment Terms. The principal balance and all accrued but unpaid interest, if any, shall be due and payable in full upon the demand of Holder.
3. Application of Payments. All payments on this Note shall be applied first to the payment of attorneys, fees, costs, and other charges to the extent, if any, provided herein; then to interest accruing hereon; and then to principal. The unpaid principal balance of this Note shall continue to bear interest until and including the date payment is received.
4. Prepayment. This Note may be prepaid in whole or in part at any time without premium or penalty.
5. Default. If default is made in the payment of principal or interest when due, and Maker fails to cure such default after ten (10) days after receiving written notice, then the whole sum of principal and accrued interest, shall at the option of the holder hereof, become immediately due and payable, anything contained herein or in any instrument now or hereafter relating to or securing the indebtedness evidenced hereby to the contrary thereof notwithstanding, time being of the essence of

this agreement, provided further, that such right to accelerate shall be in addition to any other rights or remedies available to Holder in equity or at law. Such option shall continue until all such defaults have been cured. Failure to exercise such option, or any other right the holder may have in such event, or be entitled to, shall not constitute a waiver of the right to exercise such option or any other rights in the event of any subsequent default.

6. Modifications. The undersigned and any party pledging collateral as security for the payment hereof agree that the Holder hereof may extend the time of payment or otherwise modify the terms of payment of any part or the whole of the indebtedness evidenced hereby or release and/or subordinate any security for this Note at any time at the request of anyone now or hereafter liable, and such consent shall not alter nor diminish the liability of any person or the enforceability of this Note or any security interest pledged as collateral for the payment hereof. Each and every party now or hereafter signing or endorsing this Note binds himself as a principal and not as a surety. All of the terms, covenants, provisions and conditions herein contained are made on behalf of, and shall apply to and bind the undersigned and their respective personal representatives, successors and assigns, jointly and severally.

7. Late Charge. If any payment required under this Note is not received by Holder within ten (10) days after the date on which such payment is due, Maker shall pay to Holder on demand a late charge in an amount equal to ten percent (10%) of the amount due. Maker and Holder agree that the late charge is intended to be a reasonable approximation of actual damages incurred by Holder as a result of such overdue payment, which damages are difficult to estimate. The imposition or collection of a late charge is in addition to and not in lieu of any other rights or remedies Holder may have as a result of late payment.

8. Costs of Enforcement. If, upon the occurrence of an event of default, the prevailing party shall be entitled to recover from the losing party all costs thereof, including reasonable attorneys' fees and costs of litigation. All such costs and attorneys' fee shall include, without limitation, those incurred on any appeal or review and in any proceeding under any present or future bankruptcy or similar proceeding or state receivership.

9. Interest Limitation. Interest, fees, and charges collected or to be collected in connection with the indebtedness evidenced by this Note shall not exceed the maximum, if any, permitted by applicable law. If any such law is interpreted so that any such interest, fees, or charges would exceed any such maximum, and if Maker is entitled to the benefit of such law, then (a) such interest, fees, or charges shall be reduced to the permitted maximum and (b) any sums already collected from Maker which exceed the permitted maximum shall be refunded. Holder may elect to make any such refund either by treating the payments, to the extent of the excess, as payments of principal (without application of any prepayment fee) or by making a direct payment to Maker.

10. No Security. This Note is unsecured.

11. Waiver. The Maker and endorsers hereof jointly and severally waive presentment for payment, protest, notice or protest and of non-payment of this note and agree that on default in payment of this Note, or any part, principal or interest, when due, the whole amount remaining unpaid shall, without notice of non-payment or demand of payment, immediately become due and payable.

12. Notices. Any notice to Maker under this Note shall be in writing and shall be deemed given when delivered by personal service or when placed in the U.S. Mail, postage prepaid, certified mail, return receipt requested, addressed to Maker, at the address set forth in the first paragraph of this Note or such other address as Maker may designate by written notice to Holder. Any notice to Holder under this Note shall be in writing and shall be deemed given when delivered by personal service or the day of placement in the U.S. Mails, postage prepaid, certified mail, return receipt requested, addressed to Holder at the address set forth in the first paragraph of this Note, or such other address as Holder may designate by written notice to Maker.
13. Modifications. Any modification to this Note must be set forth in writing and executed by the Maker and Holder.
14. Governing Law and Venue. This Note shall be governed by the laws, including conflicts of laws, in the State of Idaho as an agreement between residents of the State of Idaho and to be performed within the State of Idaho. Venue shall be in the Idaho State district court for Ada County, Idaho.
15. Binding Effect. This Note shall be binding upon and inure to the benefit of the parties hereto and their respective heirs, legal representatives, successors and assigns.
16. Time of Essence. All times provided for in this Note, or in any other document executed hereunder, for the performance of any act will be strictly construed, time being of the essence.
17. Remedies Cumulative. Each right, power and remedy provided for herein or now or hereafter existing in law, in equity, by statute or otherwise shall be cumulative and concurrent and shall be in addition to every other right, power or remedy provided for herein or now or hereafter existing at law, in equity, by statute or otherwise, and the exercise or beginning of the exercise or the forbearance of exercise by any the Holder of any one or more of such rights, powers or remedies shall not preclude the simultaneous or later exercise by the Holder of any or all of such other rights, powers or remedies.
18. Severability. If any term or provision of this Note shall, to any extent be determined by a court of competent jurisdiction to be invalid or unenforceable, the remainder of this Note shall not be affected thereby, and each term and provision of this Note shall be valid and be enforceable to the fullest extent permitted by law; and it is the intention of the parties that if any provision of this Note is capable of two constructions, one of which would render the provision void and the other of which would render the provision valid, the provision shall have the meaning which renders it valid.

[end of text]

This Promissory Note is executed effective the date first set forth above.

Butte Highlands JV, LLC

By: Robert K. Galt

Its: MDnGLN

EXHIBIT D

SAMPLE OF ALLOCATIONS AND DISTRIBUTIONS

Butte Highlands JV
Hypothetical allocation

Facts:

Highland Mining, LLC contributes \$15,000,000 in cash as loan and contribution.

Timberline Resources contributes \$2,000,000 in land in year 0.

All cash is spent on development in the year contributed.

In Years 2 and 3 \$20,000,000 is earned pro-rata per quarter.

At point parity is reached equalizing distribution is made to make capital accounts equal

Totals for example	Income all years	Distributions received
Highland	7,500,000	6,000,000
TLR	7,500,000	6,000,000
	15,000,000	12,000,000

	2009	2010	1/1/2011	3/31/2011	2nd Quarter
Cash	-	-	-	5,000,000	5,000,000
Land	-	2,000,000	-	2,000,000	-
Due to Highland Mining	-	(2,000,000)	2,000,000	-	-
Highland Mining Equity	-	2,000,000	(13,000,000)	(13,000,000)	4,000,000
TLR Equity	-	(2,000,000)	13,000,000	9,000,000	-
	-	(2,000,000)	(2,000,000)	(3,000,000)	1,000,000
Profit/(Loss)	-	-	-	-	-
Highland Cont/Dist	-	-	5,000,000	-	-
TLR Cont/Dist	-	-	-	-	-
Highland Loans	-	-	-	-	1,000,000
	-	-	-	-	4,000,000

Allocation:

Reasoning:

100% Highland
0% TLR
Not to parity

(2,000,000)

100% Highland
0% TLR
Not to parity

(13,000,000)

80% Highland
20% TLR
Not to parity

4,000,000
1,000,000

80% Highland
20% TLR
Not to parity

4,000,000
1,000,000

No distributions/debt payments
cash retained for W/C

At time parity is reached W/C will be readjusted

Butte Highlands JV
Hypothetical allocation

Facts:

Highland Mining, LLC cor
Timberline Resources cor
All cash is spent on devel
In Years 2 and 3 \$20,000
At point parity is reached

	3rd Quarter		4th Quarter		1st Quarter		2nd Quarter		
	6/30/2011	9/30/2011	12/31/2011	3/31/2012	6/30/2012	9/30/2012	12/31/2012	3/31/2013	6/30/2013
Cash	5,000,000	5,000,000	5,000,000	5,000,000	5,000,000	5,000,000	5,000,000	5,000,000	5,000,000
Land	2,000,000	2,000,000	2,000,000	2,000,000	2,000,000	2,000,000	2,000,000	2,000,000	2,000,000
Due to Highland Mining	(9,000,000)	(9,000,000)	(9,000,000)	(9,000,000)	(9,000,000)	(9,000,000)	(9,000,000)	(9,000,000)	(9,000,000)
Highland Mining Equity	5,000,000	5,000,000	5,000,000	5,000,000	5,000,000	5,000,000	5,000,000	5,000,000	5,000,000
TLR Equity	(3,000,000)	(3,000,000)	(3,000,000)	(3,000,000)	(3,000,000)	(3,000,000)	(3,000,000)	(3,000,000)	(3,000,000)
Profit/(Loss)	-	-	-	-	-	-	-	-	-
Highland Cont/Dist	-	-	-	-	-	-	-	-	-
TLR Cont/Dist	-	-	-	-	-	-	-	-	-
Highland Loans	-	-	-	-	-	-	-	-	-

Allocation:

Reasoning:

80% Highland	4,000,000	80% Highland	4,000,000	80% Highland	4,000,000	50% Highland	2,500,000
20% TLR	1,000,000	20% TLR	1,000,000	20% TLR	1,000,000	50% TLR	2,500,000
Not to parity		Not to parity		Parity reached		Parity	

Distributions taken project to date

Highland	-
TLR	3,000,000
Available cash for distribution	4,000,000
Highland to equalize	3,000,000
Remaining	1,000,000
0.5 Highland	500,000
0.5 TLR	500,000

STOCK SETTLEMENT AND RELEASE AGREEMENT

THIS STOCK SETTLEMENT AND RELEASE AGREEMENT (this “**Agreement**”) is made as of this 14th day of July, 2009, by and between Timberline Resources Corporation (“**Timberline**”), a Delaware corporation, and Jefferies & Company, Inc. (“**Jefferies**”).

RECITALS

WHEREAS, Jefferies provided Timberline financial advisory services in connection with a possible transaction or series of transactions involving Timberline and a target company, and was engaged by Timberline as a placement agent, arranger, or initial purchaser for the potential financing for such a transaction or transactions (the “**Services**”), pursuant to the terms of two agreements: an engagement agreement dated November 1, 2007 (the “**Advisory Engagement Agreement**”); and an engagement agreement dated April 4, 2008 (the “**Placement Agent Engagement Agreement**”), (together the “**Engagement Agreements**”) each by and between Timberline and Jefferies; and

WHEREAS, pursuant to the Engagement Agreements, Timberline was to pay Jefferies a fee of \$500,000 for a Fairness Opinion, a cash fee and warrants in the event that securities were placed, and expenses including legal fees incurred by Jefferies pursuant to the provision of the Services (collectively, the “**Fees**”); and

WHEREAS, Jefferies has issued an invoice to Timberline, Invoice number 7291 dated Oct. 29, 2008, reference number AEE87, in the total amount of \$923,956.74 for the Fees (the “**Services Invoice**”), shown in Exhibit B; and

WHEREAS, neither a transaction nor a financing envisioned in the Engagement Agreements was consummated; and

WHEREAS, Timberline and Jefferies now desire that the Fees and the Services Invoice be satisfied by issuance of shares of common stock of Timberline, par value \$0.001 (“**Common Shares**”) and payment of cash.

AGREEMENT

NOW, THEREFORE, in consideration of the foregoing and the promises and covenants contained herein, the sufficiency of which is hereby acknowledged, all parties hereto agree as follows:

A. ISSUANCE OF SHARES

1. **The Shares and Cash.** Subject to the satisfaction of the terms and conditions set forth in this Agreement, Timberline agrees to issue 950,000 Common Shares (the “**Exchange Shares**”) and pay \$50,000.00 cash (the “**Exchange Cash**”) to Jefferies in exchange for Jefferies’ release of Timberline’s payment in cash of the Fees reflected on the Services Invoice, and

Jefferies agrees to accept such Exchange Shares and Exchange Cash from Timberline as satisfaction, in full, of the Services Invoice.

2. Issuance of Shares. Timberline shall deliver the stock certificate(s) representing the Shares, registered with Timberline's Transfer Agent and delivered as set forth on Exhibit A attached hereto, free and clear from any restrictions on transfer, except those restrictions on transfer described in Section (B)(7) hereof, upon the later of: (i) three (3) business days following the execution of this Agreement by both parties or (ii) three (3) business days following the approval of the issuance of the Exchange Shares by the NYSE Amex ("**NYSE Amex**").

3. Payment of Cash. Timberline shall wire the Exchange Cash to Jefferies no later than the third business day following the execution of this Agreement by both parties. Jefferies' wiring instructions are as follows:

Bank of New York
ABA: 021000018
Account Number: 8900007001
Tax ID: 952622900
Reference: Timberline

B. REPRESENTATIONS AND WARRANTIES OF JEFFERIES

Jefferies represents, warrants and covenants (and acknowledges that Timberline is relying on such representations, warranties and covenants) that, as of the date of this Agreement:

1. Jefferies understands that, at the time Jefferies receives the Exchange Shares, (i) the Exchange Shares will not be registered under the U.S. Securities Act of 1933, as amended (the "U.S. Securities Act") or any applicable state securities laws and may not be offered or sold absent such registration or an available exemption from such registration requirements and (ii) the Exchange Shares will not be approved or disapproved by the United States Securities and Exchange Commission (the "SEC") or any state securities agency. Jefferies understands and agrees that the Exchange Shares are being issued to Jefferies in reliance upon the exemption provided under Rule 506 of Regulation D and/or section 4(2) under the U.S. Securities Act;

2. Jefferies is not an underwriter and Jefferies will acquire the Exchange Shares solely for investment purposes for its own account and not with a view to, or for, resale in connection with any distribution of securities within the meaning of the U.S. Securities Act; and the Exchange Shares will not be obtained with a view to or for the resale, distribution, subdivision or fractionalization thereof; and the undersigned has no contract, undertaking, understanding, agreement, or arrangement, formal or informal, with any person to sell, transfer, or pledge to any person the Exchange Shares; and it understands that the legal consequences of the foregoing representations and warranties to mean that it must bear the economic risk of the investment for an indefinite period of time because the Exchange Shares, at the time of receipt, will not be registered under the U.S. Securities Act, and, therefore, may be resold only if registered under the U.S. Securities Act or if an exemption from such registration requirement is available;

3. Jefferies is an “accredited investor” that satisfies one or more of the criteria set forth in Rule 501(a) of Regulation D of the U.S. Securities Act;

4. Jefferies understands that, except as provided in Section E hereof, Timberline is under no obligation to register the Exchange Shares or to cause or permit the Exchange Shares to be transferred in the absence of any such registration or exemption;

6. Jefferies has not purchased the Exchange Shares as a result of any form of general solicitation or general advertising (as such terms are used in Rule 502 (c) under Regulation D of the U.S. Securities Act);

7. Jefferies acknowledges that the Exchange Shares will be “restricted securities,” as such term is defined under Rule 144 of the U.S. Securities Act, and may not be offered, sold, transferred, pledged, or hypothecated to any person in the absence of registration under the U.S. Securities Act or an opinion of counsel that registration is not required. Without limiting the generality or application of any other covenants, representations, warranties and acknowledgements of Jefferies respecting resale of the Exchange Shares, Jefferies will not offer, sell or otherwise transfer any of such Exchange Shares directly or indirectly, unless in accordance with the following legend, which Jefferies acknowledges the certificates representing the Exchange Shares delivered pursuant to this Agreement shall bear (until such time as the Exchange Shares have been registered under the U.S. Securities Act or an opinion of counsel is received that such legend is no longer required):

“THE SECURITIES REPRESENTED HEREBY HAVE NOT BEEN REGISTERED UNDER THE UNITED STATES SECURITIES ACT OF 1933, AS AMENDED (THE “U.S. SECURITIES ACT”). THESE SECURITIES MAY BE OFFERED, SOLD, PLEDGED OR OTHERWISE TRANSFERRED ONLY (A) TO TIMBERLINE, (B) IF THE SECURITIES HAVE BEEN REGISTERED IN COMPLIANCE WITH THE REGISTRATION REQUIREMENTS UNDER THE U.S. SECURITIES ACT AND IN ACCORDANCE WITH APPLICABLE STATE SECURITIES LAWS, (C) IN COMPLIANCE WITH THE EXEMPTION FROM THE REGISTRATION REQUIREMENTS UNDER THE U.S. SECURITIES ACT PROVIDED BY RULE 144, RULE 144A OR REGULATION S THEREUNDER, IF AVAILABLE, AND IN ACCORDANCE WITH APPLICABLE STATE SECURITIES LAWS, OR (D) IN ANOTHER TRANSACTION THAT DOES NOT REQUIRE REGISTRATION UNDER THE U.S. SECURITIES ACT OR ANY APPLICABLE STATE LAWS AND REGULATIONS GOVERNING THE OFFER AND SALE OF SECURITIES, AND THE HOLDER HAS, PRIOR TO SUCH SALE, FURNISHED TO TIMBERLINE AN OPINION OF COUNSEL, OR OTHER EVIDENCE OF EXEMPTION, REASONABLY SATISFACTORY TO TIMBERLINE. HEDGING TRANSACTIONS INVOLVING THE SECURITIES REPRESENTED HEREBY MAY NOT BE CONDUCTED UNLESS IN COMPLIANCE WITH THE U.S. SECURITIES ACT.”

If Rule 144 under the U.S. Securities Act is applicable, then the undersigned may make sales of the Exchange Shares only under the terms and conditions prescribed by Rule 144 of the U.S. Securities Act or other exemptions therefrom (unless the Exchange Shares have been registered). Timberline shall use commercially reasonable efforts to cause its legal counsel to deliver an opinion or such other documentation as may reasonably be required to effect sales of the Exchange Shares under Rule 144;

8. Jefferies consents to Timberline making a notation on its records or giving instruction to the registrar and transfer agent of Timberline in order to implement the restrictions on transfer set forth and described herein;

9. Jefferies is a corporation and in good standing under the laws of its jurisdiction of incorporation; and

10. Jefferies acknowledges that Timberline has received notification from the NYSE Amex that Timberline does not currently meet the continued listing requirements of the NYSE Amex and that the common shares of Timberline could be de-listed from NYSE Amex, regardless of Timberline's commercially reasonable efforts to maintain such listing;

11. this Agreement has been duly executed and delivered by Jefferies and constitutes a legal, valid and binding obligation of Jefferies enforceable against Jefferies in accordance with its terms, except as enforcement thereof may be limited by bankruptcy, insolvency, reorganization, moratorium and other laws relating to or affecting the rights of creditors generally and except as limited by the application of equitable principles when equitable remedies are sought, and by the fact that rights to indemnity, contribution and waiver, and the ability to sever unenforceable terms, may be limited by applicable law.

C. REPRESENTATIONS AND WARRANTIES OF TIMBERLINE

Timberline represents, warrants and covenants (and acknowledges that Jefferies is relying on such representations, warranties and covenants) that, as of the date of this Agreement:

1. Timberline has been duly incorporated and is validly existing as corporation in good standing under the laws of its jurisdiction of incorporation and has the power and authority (corporate or other) to own, lease, and operate its properties and to conduct its business as so owned, leased or operated and conducted on the date of this Agreement;

2. All of the issued and outstanding shares of Timberline's common stock have been duly authorized and validly issued, are fully paid and nonassessable and have been issued in compliance with federal and state securities laws;

3. Timberline is duly qualified, registered and licensed to carry on business and is in good standing in the jurisdictions in which it carries on business or owns property where so required by the laws of that jurisdiction;

4. Timberline is not (i) in violation of any material term of or in material default under its certificate of incorporation, bylaws or other organizational document, (ii) in default (or, with the giving of notice or lapse of time, would be in default or constitute a default) (“Default”) under any material term, covenant or condition contained in any indenture, mortgage, deed of trust, loan agreement or other agreement or instrument to which Timberline is a party or by which it or any of them may be bound, or to which any of the property or assets of Timberline is subject (each, an “Existing Instrument”), or (iii) in violation of any judgment, decree or order or any statute, ordinance, rule, law or regulation applicable to Timberline, where such violation would have a material adverse effect on Timberline. Timberline’s execution, delivery and performance of this Agreement, the issuance of the Exchange Shares and the payment of the Exchange Cash (i) will not result in any material violation of the provisions of the charter or bylaws of Timberline, (ii) will not conflict with or constitute a material breach of, or Default under, or result in the creation or imposition of any security interest, mortgage, pledge, lien, charge, encumbrance or adverse claim upon any property or assets of Timberline pursuant to, or require the consent of any other party to any Existing Instrument or other third party and (iii) will not result in any violation of any law, administrative regulation or administrative or court decree applicable to Timberline. No consent, approval, authorization or other order of, or registration or filing with, any court or other governmental or regulatory authority or agency, is required for Timberline’s execution, delivery and performance of this Agreement, issuance of the Exchange Shares and payment of the Exchange Cash, except: (i) as required by the state securities or “blue sky” laws, (ii) approval of the issuance of the Exchange Shares by the NYSE Amex and (iii) for such consents, approvals, authorizations, orders, filings or registrations that have been obtained or made and are in full force and effect;

5. Timberline represents that there are no placement agent’s fees, financial advisory fees, or brokers’ commissions or similar fees or payments due to any person relating to or arising out of the issuance of the Exchange Shares under this Agreement. Timberline shall pay, and hold Jefferies harmless against, any liability, loss or expense (including, without limitation, foreseeable and documented attorney’s fees and out-of-pocket expenses) arising in connection with any such claim. Nothing herein shall be construed to hold Timberline responsible for any placement agent’s fees, financial advisory fees, or brokers’ commissions or similar fees or payments due in relation to or arising out of Jefferies’ subsequent re-sale or transfer of the Exchange Shares, which fees or commissions remain the sole obligation of Jefferies;

6. Neither Timberline nor any person acting on its behalf, has, directly or indirectly, made any offers or sales of any security or solicited any offers to buy any security, under circumstances that would require registration of any of the Exchange Shares under the U.S. Securities Act or cause this offering of the Exchange Shares to be integrated with prior offerings by Timberline for purposes of the U.S. Securities Act. Neither Timberline nor any person acting on its behalf, will take any action or steps referred to in the preceding sentence that would require registration of the offer, issuance or sale of any of the Exchange Shares under the U.S. Securities Act or cause the offering of the Exchange Shares to be integrated with other offerings other than as required by this Agreement;

7. There are no legal or governmental actions, suits or proceedings pending or, to the best of Timberline’s knowledge, threatened (i) against or affecting Timberline, (ii) which has as the subject thereof any officer or director of, or property owned or leased by, Timberline or (iii)

relating to environmental or discrimination matters, where in any such case (A) there is a reasonable possibility that such action, suit or proceeding might be determined adversely to Timberline or such officer or director, (B) any such action, suit or proceeding, if so determined adversely, would adversely affect the consummation of the transactions contemplated by this Agreement and (C) any such action, suit or proceeding is or would be material in the context of the sale of Exchange Shares.

8. Timberline has all necessary power and authority to issue and deliver the Exchange Shares; the Exchange Shares have been duly authorized, and, when duly issued and delivered to Jefferies pursuant to the terms of this Agreement, the Exchange Shares will be duly-issued, fully-paid and non-assessable securities of Timberline. None of the Exchange Shares will be issued in violation of any preemptive rights, rights of first refusal or other similar rights to subscribe for or purchase securities of Timberline;

9. this Agreement has been duly authorized by all necessary corporate action on the part of Timberline, and Timberline has full corporate power and authority to undertake its obligations under this Agreement and execute this Agreement;

10. this Agreement has been duly authorized, executed and delivered by Timberline and constitutes a valid and legally binding obligation of Timberline enforceable against it in accordance with its terms, except as enforcement thereof may be limited by bankruptcy, insolvency, reorganization, moratorium and other laws relating to or affecting the rights of creditors generally and except as limited by the application of equitable principles when equitable remedies are sought, and by the fact that rights to indemnity, contribution and waiver, and the ability to sever unenforceable terms, may be limited by applicable law;

11. no order ceasing, halting or suspending trading in securities of Timberline nor prohibiting the sale of such securities has been issued to and is outstanding against Timberline or its directors, officers or promoters, and, to the best of Timberline's knowledge, no investigations or proceedings for such purposes are pending or threatened;

12. neither Timberline nor any person acting on its or their behalf has engaged in or will engage in any form of "general solicitation" or "general advertising" (as such terms are used in Rule 502 (c) under Regulation D of the U.S. Securities Act) in the United States with respect to the Exchange Shares;

13. the shares of Timberline's common stock are registered pursuant to Section 12(b) of the Securities Exchange Act of 1934, as amended (the "Exchange Act") and are listed on the NYSE Amex, and Timberline has taken no action designed to, or likely to have the effect of, terminating the registration of the shares of common stock under the Exchange Act or delisting the shares of common stock from the NYSE Amex, nor has Timberline received any notification that the SEC is contemplating terminating such registration. Timberline represents that it has received notice of de-listing from the NYSE Amex, that the NYSE Amex has accepted Timberline's compliance plan pursuant to the rules of the NYSE Amex, and that as of the date of this Agreement Timberline is in compliance with such plan. Timberline shall cause the Exchange Shares to be listed on the NYSE Amex and shall use its commercially reasonable efforts to maintain the continued listing of its common shares on the NYSE Amex until the earlier of

twenty-four months after the execution of this Agreement or such date on which Jefferies shall have sold all the Exchange Shares.;

14. any documents filed with the SEC by Timberline, at the time they were or hereafter are filed with the SEC, complied and will comply in all material respects with the requirements of the Exchange Act;

15. since March 31, 2009, there has been no material adverse change and no material adverse development in the business, properties, operations, condition (financial or otherwise), results of operations or prospects of Timberline; and

16. until the earlier of twenty-four months after the execution of this Agreement or such date on which Jefferies shall have sold all the Exchange Shares, Timberline shall timely file all reports required to be filed with the SEC pursuant to the Exchange Act, and Timberline shall not terminate its status as an issuer required to file reports under the Exchange Act even if the Exchange Act or the rules and regulations thereunder would otherwise permit such termination.

D. RELEASE

Subject to Section G(9) below, in consideration of the issuance of the Exchange Shares and the payment of the Exchange Cash as satisfaction, in full, of the Services Invoice, Jefferies (including its officers, employees, agents, representatives, assignees, and successors) hereby releases Timberline (including its officers, employees, agents, representatives, assignees, and successors) from any and all manner of action and causes of action, suits, debts, dues, accounts, contracts, agreements, judgments, claims and demands whatever, whether in law or in equity, which now exist or may subsequently arise out of the Services Invoice or the Engagement Agreements .

E. REGISTRATION RIGHTS

Within 30 days of the date hereof, Timberline agrees to include Jefferies or its nominee as a selling shareholder of the Exchange Shares in a registration statement under the U.S. Securities Act that Timberline will file with the SEC relating to the resale under the U.S. Securities Act of the Exchange Shares, and Timberline hereby agrees to cause such registration statement to become effective as quickly as practicable but in any event within 120 days of such filing and to use reasonable best efforts to ensure that such registration statement remains effective until the earlier of twenty-four months after the execution of this Agreement or such date on which Jefferies shall have sold all the Exchange Shares.

F. INDEMNITY.

Timberline shall indemnify, defend and hold Jefferies harmless against any and all liabilities, loss, cost or damage, together with all reasonable costs and expenses related thereto (including reasonable legal and accounting fees and expenses), to the extent such are determined, by a final, non-appealable judgment by a court or arbitral tribunal, to have arisen from, related to, or connected with any untrue, inaccurate or breached statement, representation, warranty or covenant of Timberline set forth in this Agreement. Timberline undertakes for a period of 12

months after the execution of this Agreement to notify Jefferies within 2 business days of any change in any representation, warranty or covenant of Timberline set forth in this Agreement to be untrue.

Jefferies shall indemnify, defend and hold Timberline harmless against any and all liabilities, loss, cost or damage, together with all reasonable costs and expenses related thereto (including reasonable legal and accounting fees and expenses), to the extent such are determined, by a final, non-appealable judgment by a court or arbitral tribunal, to have resulted solely from Jefferies' gross negligence or willful misconduct under this Agreement.

G. MISCELLANEOUS PROVISIONS

1. Successors and Assigns. Except as otherwise provided herein, the terms and conditions of this Agreement shall inure to the benefit of and be binding upon the respective successors and assigns of the parties. Nothing in this Agreement, express or implied, is intended to confer upon any party, other than the parties hereto or their respective successors and assigns, any rights, remedies, obligations or liabilities under or by reason of this Agreement, except as expressly provided in this Agreement.

2. Governing Law. This Agreement shall be governed by and construed in accordance with the laws of the State of New York, without regards to conflict of law principles thereof.

3. Titles and Subtitles. The titles and subtitles used in this Agreement are used for convenience only and are not to be considered in construing or interpreting this Agreement.

4. Notices. All notices required or permitted hereunder shall be in writing and shall be deemed effectively given: (i) upon personal delivery to the party to be notified, (ii) when sent by confirmed telex or facsimile if sent during normal business hours of the recipient, if not, then on the next business day; (iii) five days after having been sent by registered or certified mail, return receipt requested, postage prepaid; or (iv) one day after deposit with a nationally recognized overnight courier, specifying next day delivery, with written verification of receipt, as follows:

If to Jefferies, to:	Jefferies & Company, Inc. 520 Madison Avenue New York, NY 10022 Attention: General Counsel
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If to Timberline, to:	Timberline Resources Corporation 101 E. Lakeside Coeur d'Alene, ID 83814 Attention: Randal Hardy
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5. Amendments and Waivers. Any term of this Agreement may be amended and the observance of any term of this Agreement may be waived (either generally or in a

particular instance and either retroactively or prospectively), only with the written consent of Timberline and Jefferies.

6. Severability. If one or more provisions of this Agreement are held to be unenforceable under applicable law, such provision shall be excluded from this Agreement and the balance of the Agreement shall be interpreted as if such provision were so excluded and shall be enforceable in accordance with its terms.

7. Entire Agreement. This Agreement and the documents referred to herein constitute the entire agreement among the parties and no party shall be liable or bound to any other party in any manner by any warranties, representations or covenants except as specifically set forth herein or therein.

8. Counterparts. This Agreement may be executed in two or more counterparts, each of which shall be deemed an original, but all of which together shall constitute one and the same instrument.

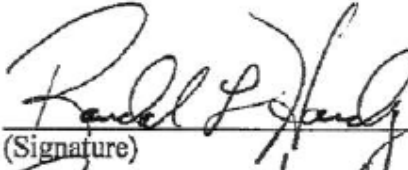
9. Material Breach of Agreement by Timberline. If prior to the earlier of twenty-four months after the execution of this Agreement or such date on which Jefferies shall have sold all the Exchange Shares, Timberline materially breaches any of the provisions of this Agreement, Jefferies shall promptly notify Timberline of any such material breach of the Agreement and demand that Timberline cure the breach. Upon receipt of the notice of a material breach of the Agreement and demand for cure from Jefferies, Timberline shall have 15 business days to cure the material breach to the satisfaction of Jefferies, not to be unreasonably withheld. If after the expiration of the 15-business-day cure period, the material breach of the Agreement has not been cured to the satisfaction of Jefferies, not to be unreasonably withheld, (A) all provisions of this Agreement except Sections F, G(2), G(4), G(6), G(9) and G(10) shall become null and void and (B) Jefferies shall be obligated to return any unsold Exchange Shares to Timberline. Upon surrender to Timberline of any unsold Exchange Shares, (A) the Service Invoice will be deemed “not satisfied”, except that the amount of Fees owed to Jefferies under the Service Invoice shall be reduced by the Exchange Cash and the value of the aggregate proceeds received by Jefferies from the sale of any Exchange Shares, and (B) Jefferies will no longer be bound by the provisions of the release of section D of this Agreement.

10. Notice of Sales. To aid Timberline in meeting its obligations under this Agreement, until the earlier of twenty-four months from the date of execution of this Agreement or until such time as Jefferies has sold all of the Exchange Shares, Jefferies agrees to provide Timberline by the end of any month in which any sales or transfers of the Exchange Shares occurs with a notice detailing the number of Exchange Shares sold and the price at which such Exchange Shares are sold and Jefferies agrees to promptly notify Timberline when all Exchange Shares have been sold.

[SIGNATURE PAGE FOLLOWS]

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

TIMBERLINE RESOURCES CORPORATION:


(Signature)

RANDAL L. Hardy
(Print)

CEO
(Title)

JEFFERIES & COMPANY, INC.:


(Signature)

Jeffrey R. Whyte
(Print)

General Counsel - Instant Bank
(Title)

EXHIBIT A

Registration and Delivery Instructions

Registration Information

Registration of the certificates representing the securities should be made exactly as follows:

Jefferies & Company, Inc.

Delivery of Certificates

The certificates representing the securities is to be delivered as follows:

By overnight courier to:

Mark Sahler
Jefferies & Company, Inc.
Harborside Financial Center
Plaza 3, Suite 705
Jersey City, New Jersey 07311

Services Invoice

Page 1 of 1

EXHIBIT 21

LIST OF SUBSIDIARIES OF TIMBERLINE RESOURCES CORPORATION

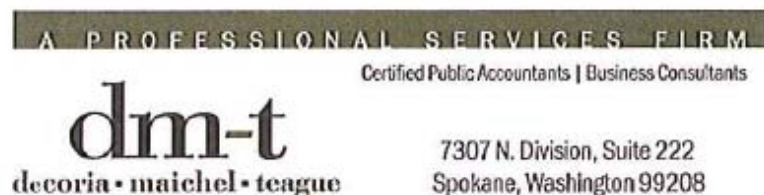
Timberline Drilling Inc., Idaho

World Wide Exploration, S.A. de C.V., Mexico

Small Mine Development, Inc., Delaware

Staccato Gold Resources Ltd., British Columbia, Canada

BH Minerals USA Inc., Colorado



CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We hereby consent to the incorporation by reference in the Registration Statement No. 333-153328 on Form S-8 of Timberline Resources Corporation and Registration Statement Nos. 333-161318 and 333-162631 on Form S-3 of our report dated December 16, 2010, with respect to the consolidated balance sheets of Timberline Resources Corporation as of September 30, 2010 and 2009, and the related consolidated statements of operations and comprehensive income (loss), changes in stockholders' equity and cash flows for the years then ended, which report appears in the September 30, 2010 annual report on Form 10-K of Timberline Resources Corporation.

DeCoria, Maichel & Teague P.S.

DeCoria, Maichel & Teague, P.S.
Spokane, Washington
December 16, 2010

EXHIBIT 31.1

CERTIFICATION

I, Randal Hardy, certify that:

1. I have reviewed this Annual Report on Form 10-K of Timberline Resources Corporation,
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: December 17, 2010

By: /s/ Randal Hardy

Randal Hardy
Chief Executive Officer & Chief Financial Officer
Principal Executive and Financial Officer

EXHIBIT 31.2

CERTIFICATION

I, Craig Crowell, certify that:

1. I have reviewed this Annual Report on Form 10-K of Timberline Resources Corporation,
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: December 17, 2010

By: /s/ Craig Crowell

Craig Crowell
Chief Accounting Officer
Principal Accounting Officer

EXHIBIT 32.1

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report of Timberline Resources Corporation (the “Company”) on Form 10-K for the fiscal year ended September 30, 2010, as filed with the Securities and Exchange Commission on the date hereof (the “Report”), I, Randal Hardy, Chief Executive Officer and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: December 17, 2010

By: /s/ Randal Hardy

Randal Hardy
Chief Executive Officer & Chief Financial Officer
Principal Executive and Financial Officer

The foregoing certification is being furnished solely pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Section 1350 of Chapter 63 of Title 18 of the United States Code) and is not being filed as part of the Report or as a separate disclosure document.

EXHIBIT 32.2

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report of Timberline Resources Corporation (the “Company”) on Form 10-K for the fiscal year ended September 30, 2010, as filed with the Securities and Exchange Commission on the date hereof (the “Report”), I, Craig Crowell, Chief Accounting Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934;
and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: December 17, 2010

By: /s/ Craig Crowell

Craig Crowell
Chief Accounting Officer
Principal Accounting Officer

The foregoing certification is being furnished solely pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Section 1350 of Chapter 63 of Title 18 of the United States Code) and is not being filed as part of the Report or as a separate disclosure document.