



FOCUS DISCIPLINE GROWTH

Annual Report 2010

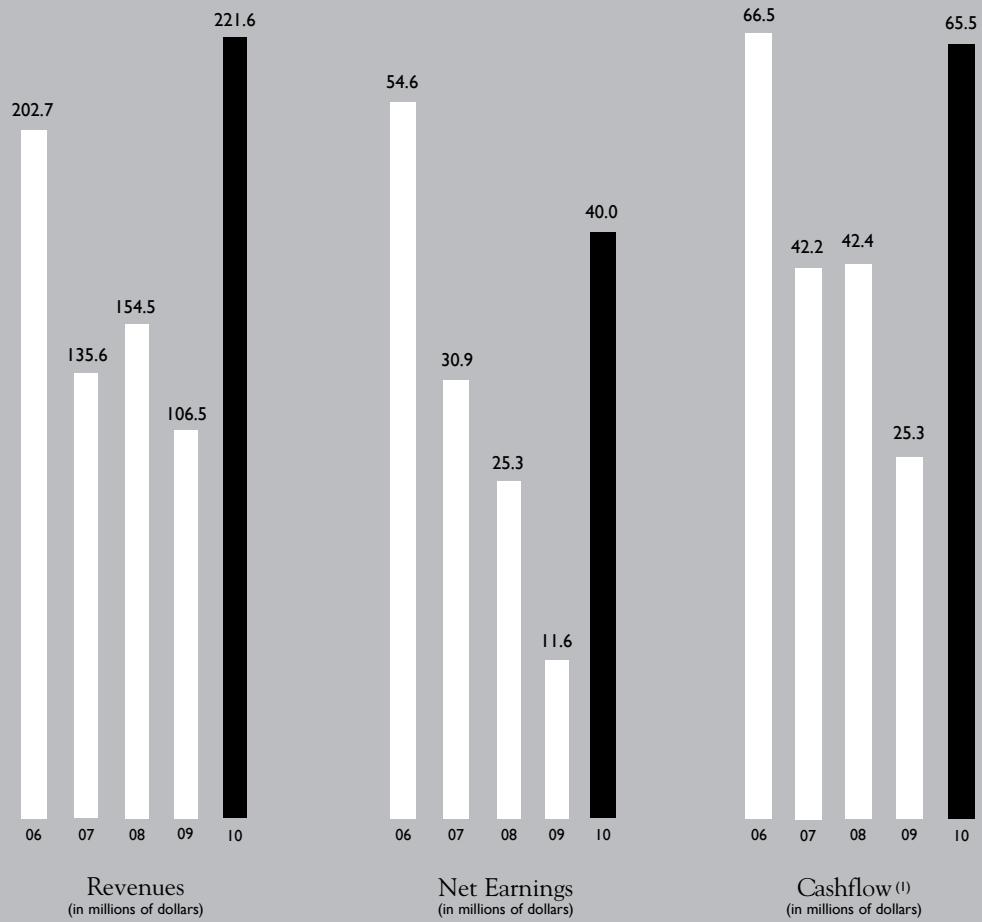
Total Energy Services Inc. ("Total Energy" or the "Company") is a growth oriented energy services company based in Calgary, Alberta. Through various operating divisions and wholly-owned subsidiaries, Total Energy is involved in three businesses: contract drilling services, rentals and transportation services and the fabrication, sale, rental and servicing of new and used natural gas compression equipment. Together these businesses provide a platform for building long-term shareholder value. Total Energy has achieved its growth by maintaining a disciplined acquisition strategy and undertaking strategic internal growth.

The shares of Total Energy are listed and trade on the Toronto Stock Exchange under the symbol TOT.

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FINANCIAL HIGHLIGHTS



(1) Cashflow means cash provided by operations before changes in non-cash working capital items.



REPORT TO SHAREHOLDERS

2010 was a positive year for Total Energy. The global financial and economic challenges that began in 2008 and continued through 2009 resulted in a very challenging period for Canadian energy services firms, with industry activity levels in 2009 reaching multi-year lows. Total was well positioned going into and during this difficult period and the strength of its balance sheet permitted the Company to pursue attractive growth opportunities despite very challenging financial market conditions. In January 2010, Total Energy completed the acquisition of DC Energy Services LP, which was the largest acquisition ever completed by the Company. This timely addition of quality people and equipment to Total Energy's Rental and Transportation Services segment, Total Oilfield Rentals LP, further positioned Total Energy to benefit from the recovery in industry activity levels that occurred over the course of 2010. In addition to the \$44.2 million acquisition of DC Energy, Total Energy invested an additional \$27.7 million during 2010 in new capital assets.

2010 represented a period of significant change for Total Energy's Gas Compression Services division, Bidell Equipment LP. Despite a difficult natural gas price environment, Bidell took steps to add significant management capacity so as to more ably pursue opportunities to grow its packaging, parts and service and rental businesses arising from significant changes within the Canadian compression marketplace that have occurred over the past few years. While much work remains to be done, Bidell is now the second largest

natural gas compression company in Canada. In early 2010, Bidell received a United States patent for its proprietary NOMAD™ line of large horsepower mobile natural gas compression packages and increasing demand for the NOMAD™ helped sustain Bidell during more challenging industry times.

In 2010, Total Energy's Contract Drilling Services division, Chinook Drilling, invested in additional equipment, including two top drives, to make its fleet of telescopic double rigs more competitive for horizontal drilling projects. Such investment began to pay off as Western Canadian drilling activity steadily increased through 2010.

LOOKING FORWARD

Western Canadian activity levels during the first quarter of 2011 have been strong, driven by horizontal drilling and multi-stage fracturing completion activity targeting oil and liquids rich natural gas. Canadian oil and natural gas producers have generally increased their capital spending plans for 2011 relative to 2010.

In January 2011, Total Energy announced a preliminary 2011 capital budget of \$21.3 million, which budget was increased to \$28.3 million in March. A \$69 million unsecured convertible debenture offering completed by Total Energy in February 2011 combined with a \$35 million bank credit facility secured only by cash on hand, inventory and receivables, provides Total Energy with substantial financial capacity and flexibility to pursue further growth opportunities as they may arise.

On behalf of the Board of Directors and Management of Total Energy, I would like to thank our employees for their hard work and continued focus on safety during this busy winter season.

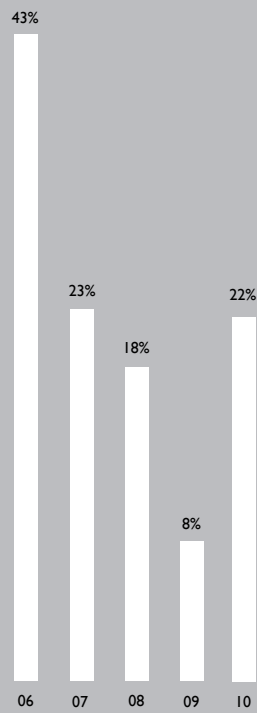


DANIEL K. HALYK

President and Chief Executive Officer
March 2011



FINANCIAL HIGHLIGHTS



Return on Average Equity ⁽¹⁾

⁽¹⁾ Return on average equity is calculated as follows:
 Net earnings divided by (opening Shareholders' equity plus ending Shareholders' equity divided by two).

FIVE YEAR COMPARISON

RESULTS (thousands of dollars, except per share data)	2010	2009	2008	2007	2006
Revenue	221,640	106,509	154,482	135,584	202,666
EBITDA ⁽¹⁾	67,623	24,058	47,097	39,682	72,273
Operating earnings ⁽¹⁾	44,042	9,741	30,806	25,437	59,020
Cash provided by operations	31,015	32,151	47,352	24,849	72,201
Cashflow ⁽¹⁾	65,473	25,366	42,412	42,160	66,544
Net earnings	39,955	11,640	25,333	30,858	54,577
Interest expense ⁽²⁾	3,332	1,520	2,510	2,384	1,604
Depreciation	20,377	13,211	13,889	11,255	10,731
Capital expenditures, net ⁽³⁾	24,069	15,231	27,981	19,317	28,200
Earnings per share - diluted	1.27	0.40	0.86	1.04	1.82
EBITDA per share - diluted ⁽¹⁾	2.15	0.83	1.60	1.33	2.42
Cashflow per share - diluted ⁽¹⁾	2.08	0.87	1.44	1.42	2.23

FINANCIAL POSITION

Working capital ⁽⁴⁾	70,409	29,493	7,254	13,438	15,907
Total assets	346,597	234,774	247,515	228,617	213,648
Long-term debt	72,500	35,713	13,521	21,383	13,545
Shareholder's equity	207,438	155,629	147,376	134,796	136,686

(1) Operating earnings are earnings before reorganization costs, gain (loss) on sale of equipment and income taxes. EBITDA means earnings before interest, taxes, depreciation and amortization and is equal to earnings before income taxes plus interest on long-term debt plus other interest expense plus depreciation. Cashflow means cash provided by operations before changes in non-cash working capital items. Operating earnings, EBITDA and cashflow are not recognized measures under Canadian generally accepted accounting principles ("GAAP"). Management believes in addition to net earnings, operating earnings, EBITDA and cashflow are useful supplemental measures as they provide an indication of the results generated by the Company's primary business activities prior to consideration of how those activities are financed, amortized or how the results are taxed in various jurisdictions as well as the cash generated by the Company's primary business activities without consideration of the timing of the monetization of non-cash working capital items. Investors should be cautioned, however, that operating earnings, EBITDA and cashflow should not be construed as an alternative to net earnings determined in accordance with GAAP as an indicator of Total Energy's performance. Total Energy's method of calculating operating earnings, EBITDA and cashflow may differ from other organizations and, accordingly, operating earnings, EBITDA and cash flow may not be comparable to measures used by other organizations.

(2) Interest expense is other interest expense plus interest on long-term debt.

(3) Excludes the acquisition of DC Energy Services LP in January 2010.

(4) Working capital equals current assets minus current liabilities.

MANAGEMENT'S DISCUSSION AND ANALYSIS ("MD&A")

The following MD&A, dated March 10, 2011, focuses on key statistics from the consolidated financial statements of Total Energy Services Inc. (the "Company" or "Total Energy") and pertains to known risks and uncertainties relating to the energy services industry. This discussion should not be considered all-inclusive, as it excludes changes that may occur in general economic, political and environmental conditions. This discussion and analysis of the financial condition and results of operations for the year ended December 31, 2010, should be read in conjunction with the audited annual consolidated financial statements for the year ended December 31, 2010 and related notes and material contained in other parts of the 2010 Annual Report as well as the Company's Annual Information Form ("AIF"). Additional information relating to Total Energy, including the Company's AIF, may be found on SEDAR at www.sedar.com. Unless otherwise indicated, all dollar amounts presented herein are in Canadian dollars.

FORWARD-LOOKING STATEMENTS

Certain information and statements contained in this MD&A constitute forward-looking information, including the anticipated costs associated with the purchase of capital equipment, expectations concerning the nature and timing of growth within the various business divisions operated through affiliates of Total Energy, expectations respecting the competitive position of such business divisions, expectations concerning the financing of future business activities, statements as to future economic and operating conditions and expectations regarding the payment of dividends in the future. Readers should review the cautionary statement respecting forward-looking information that appears below.

The information and statements contained in this MD&A that are not historical facts are forward-looking statements. Forward-looking statements (often, but not always, identified by the use of words such as "seek", "plan", "continue", "estimate", "project", "predict", "potential", "targeting", "intend", "could", "might", "should", "believe", "expect", "may", "anticipate" or "will" and similar expressions) may include plans, expectations, opinions, or guidance that are not statements of fact. Forward-looking statements are based upon the opinions, expectations and estimates of management as at the date the statements are made and are subject to a variety of risks and uncertainties and other factors that could cause actual events or outcomes to differ materially from those anticipated or implied by such forward-looking statements. These factors include, but are not limited to, such things as changes in industry conditions (including the levels of capital expenditures made by oil and gas producers and explorers), the credit risk to which the Company is exposed in the conduct of its business, fluctuations in prevailing commodity prices or currency and

interest rates, the competitive environment to which the various business divisions are, or may be, exposed in all aspects of their business, the ability of the Company's various business divisions to access equipment (including parts) and new technologies and to maintain relationships with key suppliers, the ability of the Company's various business divisions to attract and maintain key personnel and other qualified employees, various environmental risks to which the Company's business divisions are exposed in the conduct of their operations, inherent risks associated with the conduct of the businesses in which the Company's business divisions operate, timing and costs associated with the acquisition of capital equipment, the impact of weather and other seasonal factors that affect business operations, availability of financial resources or third-party financing and the impact of new laws and regulations or changes in existing laws, regulations or administrative practices on the part of regulatory authorities, including without limitation taxation and environmental laws and regulations and changes in how such laws and regulations are interpreted and enforced. Forward-looking information respecting the anticipated costs associated with the purchase of capital equipment are based upon historical prices for various classes of equipment, expectations relating to the impact of inflation on the future cost of such equipment and management's views concerning the negotiating position of the Company and its affiliates. Forward-looking information concerning the nature and timing of growth within the various business divisions is based on the current budget of the Company (which is subject to change), factors that affected the historical growth of such business divisions, sources of historic growth opportunities and expectations relating to future economic and operating conditions. Forward-looking information concerning the future competitive position of the Company's business divisions is based upon the current competitive environment in which those business divisions operate, expectations relating to future economic and operating conditions, current and announced build programs and other expansion plans of other organizations that operate in the energy service business. Forward-looking information concerning the financing of future business activities is based upon the financing sources on which the Company and its predecessors have historically relied and expectations relating to future economic and operating conditions. Forward-looking information concerning future economic and operating conditions is based upon historical economic and operating conditions, opinions of third-party analysts respecting anticipated economic and operating conditions. Although management of the Company believes that the expectations reflected in such forward looking statements are reasonable, it can give no assurance that such expectations will prove to have been correct. Accordingly, readers should not place undue reliance upon any of the forward-looking information set out in this MD&A. All of the forward looking statements of the Company contained in this MD&A are expressly qualified, in their entirety, by this cautionary statement. The various risks to which the Company is exposed are described in additional detail in this MD&A under the heading "Risk Factors" below and in the Company's AIF. Except as required by law, the Company disclaims any intention or obligation to update or revise any forward-looking information or statements, whether as a result of new information, future events or otherwise.

RESPONSIBILITY OF MANAGEMENT AND THE BOARD OF DIRECTORS

Management is responsible for the information disclosed in this MD&A and the accompanying audited consolidated financial statements, and has in place appropriate information systems, procedures and controls to ensure that information used internally by management and disclosed externally is materially complete and reliable. In addition, the Company's Audit Committee, on behalf of the Board of Directors, provides an oversight role with respect to all public financial disclosures made by the Company, and has reviewed and approved this MD&A and the accompanying audited consolidated financial statements.

DISCLOSURE CONTROLS AND PROCEDURES AND INTERNAL CONTROL OVER FINANCIAL REPORTING

The Chief Executive Officer and the Chief Financial Officer, together with other members of management (collectively, the "Officers"), have designed the Company's disclosure controls and procedures in order to provide reasonable assurance that the information required to be disclosed by the Company and its consolidated divisions and subsidiaries in its filings or other reports submitted by it under securities legislation is in compliance with the time periods specified in the securities legislation. These disclosure controls and procedures include controls and procedures which have been designed to ensure that the information required to be disclosed by the Company and

its consolidated divisions and subsidiaries in its filings or other reports submitted by it under securities legislation is accumulated and communicated to the Officers and others within those entities to allow timely decisions regarding required disclosure.

Disclosure Controls and Procedures

The Company's disclosure controls and procedures are designed to provide reasonable assurance that information required to be disclosed by the Company is reported within the time periods specified under securities laws, and include controls and procedures that are designed to ensure that information is communicated to management of Total Energy, including the Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosure. An evaluation of the effectiveness of the Company's disclosure controls and procedures (as defined in Multilateral Instrument 52-109, Certification of Disclosure in Issuers' Annual Financial and Interim Filings) was conducted as at December 31, 2010. Based on that evaluation, the Chief Executive Officer and the Chief Financial Officer of Total Energy have concluded that the design and operation of the Company's disclosure controls and procedures were effective as at December 31, 2010.

Internal Control Over Financial Reporting

The Chief Executive Officer and Chief Financial Officer of Total Energy are responsible for establishing and maintaining adequate internal control over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with Canadian generally accepted accounting principles ("GAAP"). The Chief Executive Officer and Chief Financial Officer of Total Energy directed the assessment of the design and operating effectiveness of the Company's internal control over financial reporting as at December 31, 2010 and based on that assessment determined that the Company's internal control over financial reporting was, in all material respects, appropriately designed and operating effectively.

While the Officers have designed the Company's disclosure controls and procedures and internal controls over financial reporting, they expect that these controls and procedures will not prevent all errors and fraud. A control system, no matter how well conceived or operated, can only provide reasonable, not absolute, assurance that the objectives of the control system are met.

Changes in Internal Control over Financial Reporting

During the quarter ended December 31, 2010 the Rentals and Transportation services division implemented a new Enterprise Resource Planning ("ERP") system. The change in ERP system and related processes has resulted in a change in internal control over financial reporting for this division.

Management has designed and implemented internal controls for the new ERP system. The design and operating effectiveness of these internal controls have been assessed and it has been determined that the internal controls are appropriately designed and operating effectively.

NON-GAAP MEASURES

Operating earnings are earnings before reorganization costs, gain (loss) on disposal of equipment and income taxes. EBITDA means earnings before interest, taxes, depreciation and amortization and is equal to earnings before income taxes plus interest on long-term debt plus other interest expense plus depreciation. Cashflow means cash provided by operations before changes in non-cash working capital items. Operating earnings, EBITDA and cashflow are not recognized measures under GAAP. Management believes that in addition to net earnings, operating earnings, EBITDA and cashflow are useful supplemental measures as they provide an indication of the results generated by the Company's primary business activities prior to consideration of how those activities are financed, amortized or how the results are taxed in various jurisdictions as well as the cash generated by the Company's primary business activities without consideration of the timing of the monetization of non-cash working capital items. Readers should be cautioned, however, that operating earnings, EBITDA and cashflow should not be construed as an alternative to net earnings determined in accordance with GAAP as an indicator of Total Energy's performance. Total Energy's method of calculating operating earnings, EBITDA and cashflow may differ from other organizations and, accordingly, operating earnings, EBITDA and cashflow may not be comparable to measures used by other organizations. Reconciliations of these non-GAAP measures to the most directly comparable GAAP measure is outlined below.

Operating earnings (in thousands of Canadian dollars)	Three months ended	Three months ended	Twelve months ended	Twelve months ended
	Dec. 31, 2010	Dec. 31, 2009	Dec. 31, 2010	Dec. 31, 2009
Net earnings	\$ 16,541	\$ 2,131	\$ 39,955	\$ 11,640
Add back (deduct):				
Reorganization costs	–	–	–	890
Loss / (gain) on disposal of equipment	663	(167)	128	(476)
Income tax expense (recovery)	1,369	(842)	3,959	(2,313)
Operating earnings	\$ 18,573	\$ 1,122	\$ 44,042	\$ 9,741

EBITDA (in thousands of Canadian dollars)	Three months ended	Three months ended	Twelve months ended	Twelve months ended
	Dec. 31, 2010	Dec. 31, 2009	Dec. 31, 2010	Dec. 31, 2009
Net earnings	\$ 16,541	\$ 2,131	\$ 39,955	\$ 11,640
Add back (deduct):				
Depreciation	5,572	3,659	20,377	13,211
Other interest	68	165	190	599
Interest on long-term debt	806	250	3,142	921
Income tax expense (recovery)	1,369	(842)	3,959	(2,313)
EBITDA	\$ 24,356	\$ 5,363	\$ 67,623	\$ 24,058

Cashflow (in thousands of Canadian dollars)	Three months ended	Three months ended	Twelve months ended	Twelve months ended
	Dec. 31, 2010	Dec. 31, 2009	Dec. 31, 2010	Dec. 31, 2009
Cash provided by operations	\$ 9,576	\$ 3,920	\$ 31,015	\$ 32,151
Add back (deduct):				
Changes in non-cash working capital items	14,816	782	34,458	(6,785)
Cashflow	\$ 24,392	\$ 4,702	\$ 65,473	\$ 25,366

BUSINESS OF THE COMPANY

Total Energy is a public energy services company based in Calgary, Alberta. Through its operating divisions and its wholly owned limited partnerships, Bidell Equipment Limited Partnership and Total Oilfield Rentals Limited Partnership, Total Energy is involved in three businesses: contract drilling services ("Chinook Drilling" or "Chinook"), the rental and transportation of equipment used in the drilling, completion and production of oil and natural gas wells ("Total Oilfield Rentals") and the fabrication, sale, rental and servicing of new and used natural gas compression equipment ("Bidell Equipment" or "Bidell"). Substantially all of the operations of the Company are conducted within the Western Canadian Sedimentary Basin ("WCSB"), although Total Energy investigates opportunities from time to time to expand its operations outside of the WCSB. Bidell generates international sales from its Calgary based facility.

VISION, CORE BUSINESS AND STRATEGY

Total Energy is focused on building sustainable value for its shareholders through the disciplined management of its operations and a commitment to growing its business in a capital efficient manner. Historically, Total Energy focused on the WCSB and intentionally levered its business more towards the exploration, development and production of natural gas than conventional oil. The Company has done this by its focus on establishing significant operations in northwestern Alberta and northeastern British Columbia (which is considered to be a relatively undeveloped natural gas prone area) and its involvement in the natural gas compression business. In 2007, Total Energy began to expand its geographical presence in the WCSB to include areas prone to oil exploration and development and to increase its exposure to unconventional resource development. In particular, emphasis was placed on expanding Total Energy's presence in British Columbia and Saskatchewan. With the recent application of horizontal drilling and multistage fracturing technologies to conventional oil areas of the WCSB, Total Energy's exposure to oil directed exploration, development and production activities has increased significantly. Management believes that Total Energy's existing business divisions provide a platform for building long-term shareholder value. Total Energy has achieved its growth by maintaining a disciplined acquisition strategy and undertaking measured and strategic organic growth. The Company intends to achieve ongoing expansion through organic growth and selective acquisitions.

Generally, the Company's business strategy and marketing plans and strategy are as follows:

Contract Drilling Services: The Company has targeted the sub-4000 meter vertical depth market in western Canada. Currently the Company operates a fleet of 14 rigs all constructed in 1997 or later. Of these rigs, 12 are Rigmaster telescopic doubles rated to vertical depths of up to 3,400 meters and two are Failing 3500 singles rated to 1,200 meters. The Company is focused on establishing a rig fleet size of 15-20 rigs to obtain the marketing and operational efficiencies enjoyed by a larger fleet. The Company expects to pursue the growth of its fleet through organic growth and the acquisition of modern and efficient equipment that is complementary to its existing fleet in an effort to distinguish its equipment from the competition and attract quality operations personnel.

Rentals and Transportation Services: Historically northern Alberta and northeastern British Columbia were the primary markets for the Company's rentals and transportation services. In the fourth quarter of 2007, this division expanded its operations into southeastern Saskatchewan. On January 15, 2010 the Company completed the acquisition of DC Energy Services LP ("DC Energy") which added two branch locations in Alberta (Drayton Valley and Red Deer) and increased its rental equipment fleet and heavy truck fleets by 80% and 27% respectively. The Company now operates out of 19 locations throughout Western Canada and currently owns and operates approximately 8,000 pieces of rental equipment, net of certain equipment that was disposed of during the fourth quarter of 2010 due to low utilization, as well as a modern fleet of 101 heavy trucks. The Company intends to maintain a modern and high quality equipment base supported by an extensive branch network to maintain a significant presence in its target market. The Company intends to pursue opportunities, both internal and acquisition, to increase its market share in its existing areas of operation and to further expand its geographic presence within the WCSB. The Company is also examining opportunities to expand its product and service offering within the WCSB and to expand its operations outside of the WCSB.

Gas Compression Services: The Company has historically targeted the sub-3000 horsepower gas compression market in western Canada. The Company has expanded its market to include international sales. The Company has and will continue to compete with its larger competitors by providing quality equipment and maintaining an efficient business model. The Company has also increased its in-house engineering capabilities in order to focus on developing proprietary equipment designs that provide solutions to its customers. Total Energy has applied for patent protection in Canada, the United States and certain other international jurisdictions for its proprietary trailer-mounted compression package which is branded the NOMAD™ and in January 2010 received a United States patent in respect of this technology. The Company intends to grow its natural gas compression rental business and, as such, expects to increase the amount of total horsepower in its rental fleet. During 2010 the Company expanded its parts and service business in the WCSB and currently operates out of 11 locations throughout Alberta, British Columbia and Saskatchewan.

OVERALL PERFORMANCE

The fourth quarter of 2010 was much improved from the prior year comparable quarter. The Company achieved a 166% increase in revenue from the prior year comparable quarter due primarily to the acquisition of DC Energy in January 2010 and increased business activity in all three divisions. The Company recorded earnings before income taxes of \$17.9 million in the fourth quarter of 2010 versus \$1.3 million for the prior year comparable period.

The Company's financial condition remains strong. Total assets increased by \$111.8 million during 2010, due primarily to the DC Energy acquisition in the first quarter of 2010, while bank debt (long-term debt including the current portion thereof) increased by only \$28.8 million during this period. Shareholders' equity increased by \$51.8 million, or 33%, during 2010.

KEY PERFORMANCE DRIVERS

Total Energy believes the following key performance drivers are critical to the success of its business.

- Oil and natural gas prices and the resulting cash flows, access to debt and equity financing and capital expenditures of its customers, the exploration and development companies that operate in the WCSB and, to a lesser extent, in other markets in which the Company's Gas Compression Services division competes.
- The expectations of its customers as to future oil and natural gas prices.
- The expectations of its customers as to oil and natural gas exploration and development prospects in the WCSB.
- The prevailing competitive conditions in each of the business segments in which Total Energy competes.
- The general state of global and national financial markets which impact the Company's access to debt and equity, which in turn affects the Company's cost of capital and economic rate of return on the Company's assets.
- Weather, which impacts both the ability to operate in the WCSB, as well as the overall demand for natural gas and heating oil.
- Effect of non-market forces such as government royalty and taxation policy, government incentives for renewable energy and regulatory changes, which create market uncertainty and affect industry activity levels.
- Access to, and retention of, qualified personnel.
- Ongoing technological developments that influence resource development.

There are several key performance measures the Company uses to monitor and assess its performance relative to the key performance drivers, the implementation of its strategy, and the achievement of its goals and vision. Such measures include:

- Return on invested capital and return on equity.

- Safety and environmental stewardship. The Company has a health, safety and environmental management policy in place within each of its operating divisions. Targets and objectives are set within those policies.

CAPABILITY TO DELIVER RESULTS

Non-Capital Resources

People are the most critical non-capital resource required in order for the Company to achieve its goals set out in its strategic plan, particularly during periods of robust industry conditions when competition for skilled labour is greatest. The Company is continually evaluating its human resources levels to ensure that it has adequate human resources to meet its business requirements, including during extended periods of industry weakness when staffing levels need to be adjusted lower in the face of lower demand for the Company's products and services. In addition, succession planning is ongoing in order to mitigate the impact of planned or unplanned departures of key personnel. The Company believes that it presently has sufficient human resources to successfully operate its business and to execute its strategic plan.

Capital Resources

The Company has the necessary working capital to meet its current obligations and commitments and has no off-balance sheet financing arrangements. In order to finance future growth, Total Energy anticipates utilizing a combination of working capital, cashflow, existing and new debt facilities and new equity issuances.

Systems and Processes

The Company's operational systems and processes are continually reviewed by management. The Company periodically evaluates existing systems and develops new ones as required. In 2009 the Company upgraded its enterprise resource planning system in Bidell to better position Bidell for continued growth. During 2010 the Company integrated DC Energy into the Company's Rentals and Transportation division. As part of the integration this division's accounting system was also upgraded.

In addition to certain risks, which are explained under the heading "Risk Factors" below and in the Company's AIF, the following factors impact Total Energy's business:

Seasonality and Cyclicity

The Company's business is cyclical due to the nature of its customers' cash flows and capital expenditures. Customers' cash flows and capital expenditures are in turn affected by, among other things, oil and gas prices, access to capital, the prospects for oil and gas exploration and development in the WCSB and economics of oil and gas exploration and production in the WCSB compared to the economics of international opportunities. The Company currently has no material long-term contracts in place for the provision of its equipment and services.

Seasonality impacts the Company's operations. The Company's operations are carried on in the WCSB. The ability to move heavy equipment in the Canadian oil and natural gas fields is dependent on weather conditions. As warm weather returns in the spring, the winter's frost comes out of the ground rendering many secondary roads incapable of supporting the weight of heavy equipment until such roads have thoroughly dried out. The duration of this "spring breakup" has a direct impact on the Company's activity levels. In addition, many exploration and production areas in northern Canada are accessible only in winter months when the ground is frozen hard enough to support equipment. The timing of freeze up and spring breakup affects the ability to move equipment in and out of these areas. As a result, late March through May is traditionally the Company's slowest period.

Trends and Outlook

The Company remains cautious regarding the near to medium term global economic environment. However, continued modest improvements in general economic conditions and energy prices, particularly oil and

natural gas liquids prices and current industry activity levels in the WCSB give rise to optimism. The Company believes that long-term fundamentals require continued exploration and development in the WCSB and elsewhere, particularly in respect of unconventional oil and natural gas reserves, to meet North American and world-wide demand for oil and natural gas. Increased focus on the development of unconventional oil and natural gas resources in the WCSB is expected to continue to drive activity in the future. The application of horizontal drilling and multi-stage fracturing completion technologies to WCSB oil resources has significantly increased drilling and completion activity in the WCSB targeting oil. According to Canadian Association of Drilling Contractors (‘‘CAODC’’) natural gas well completions accounted for approximately 43% of the wells drilled in the WCSB during 2010 as compared to 54% and 60% for the comparable periods in 2009 and 2008. As a result, the Company’s revenue base has become more balanced between oil and natural gas related activities whereas historically natural gas drilling and production activity was the primary driver of the Company’s revenues. The oil and gas service industry is highly reliant on the levels of capital expenditures made by oil and gas producers and explorers to find and produce oil and natural gas. These companies base their capital expenditures on several factors, including but not limited to current and expected hydrocarbon prices, exploration and development prospects and access to capital. Activity levels are ultimately dependent on these above and other factors. Industry activity levels steadily improved in 2010 as compared to 2009. Exploration and development companies have generally increased their 2011 WCSB capital budgets compared to 2010 capital expenditure levels and, as such, current indications are that WCSB industry activity levels will be relatively strong during 2011 driven primarily by oil and liquids rich natural gas drilling and completion activities.

Governmental and Environmental Regulation and Risk Management

The Company has a comprehensive insurance and risk management program in place to protect its assets, operations and employees. The Company also has programs in place to ensure it meets or exceeds current safety and environmental standards. The Company has safety and environmental personnel responsible for maintaining and developing the Company’s policies and monitoring the Company’s operations in each division to ensure they are in compliance with such policies and applicable legislation. The safety and environmental personnel report to the divisional General Managers and directly to the Vice President of Operations of the Company.

SELECTED FINANCIAL INFORMATION

Selected annual financial information derived from the audited consolidated financial statements of the Company for the three most recently completed financial years is set forth below and is prepared in accordance with GAAP.

(in thousands of dollars except per share amounts)	Year Ended Dec. 31, 2010	Year Ended Dec. 31, 2009	Year Ended Dec. 31, 2008
Revenue	\$ 221,640	\$ 106,509	\$ 154,482
Cash provided by operations	31,015	32,151	47,352
Cashflow ⁽¹⁾	65,473	25,366	42,412
Net earnings	39,955	11,640	25,333
Per share (basic)	1.30	0.40	0.86
Per share (diluted)	1.27	0.40	0.86
Dividends declared per share	0.13	0.06	–
Total assets	346,597	234,774	247,515
Long-term liabilities	75,514	35,713	13,521
(excluding current portions of long-term debt, current obligations under capital leases and future income taxes and deferred tax credit)			

(1) Refer to ‘‘Non-GAAP Measures’’ for further information

In 2010 the Company experienced higher demand for its products and services in all of its divisions and acquired DC Energy. Overall revenue for the Company increased by 108% in 2010 versus 2009 and was 43% higher than in 2008.

Cash provided by operations was 4% lower than 2009 and 35% lower than 2008 due primarily to higher accounts receivable balances at the end of 2010. Accounts receivable balances increased in 2010 as compared with 2009 and 2008 due to a substantial increase in revenues on account of the DC Energy acquisition in January 2010 and higher overall industry activity levels. Cashflow was 158% higher than 2009 and 54% higher than in 2008 due primarily to higher net earnings. Net earnings in 2010 were 243% and 58% higher than 2009 and 2008 respectively. The increase in net earnings was due primarily to increased earnings before income taxes due to the DC Energy acquisition and higher overall industry activity levels in 2010.

The Company's total assets have increased by 40% since 2008. This increase was due primarily to acquisition of DC Energy and organic growth throughout the Company. Long-term debt has increased by 458% since 2008. This is due primarily to the reclassification of bank indebtedness to long-term debt in 2009 and the DC Energy acquisition in 2010.

RESULTS OF OPERATIONS

Consolidated Revenue

Revenues increased 166% to \$72.7 million for the three months ended December 31, 2010 versus \$27.3 million for the same period in 2009 and increased 108% to \$221.6 million for the year ended December 31, 2010 versus \$106.5 million for the same period in 2009.

DIVISIONAL REVENUE

Divisional revenues for the three months ended December 31, 2010 were \$13.1 million for Contract Drilling Services, \$36.6 million for Rentals and Transportation Services and \$23.1 million for Gas Compression Services. Divisional revenues for the year ended December 31, 2010 were \$41.1 million for Contract Drilling Services, \$118.3 million for Rentals and Transportation Services and \$62.3 million for Gas Compression Services.

Contract Drilling Services

The revenue reported from Total Energy's Contract Drilling Services division increased by 83% to \$13.1 million for the three months ended December 31, 2010 as compared to \$7.1 million for the same period in 2009, and increased by 125% to \$41.1 million for the year ended December 31, 2010 as compared to \$18.3 million for the same period in 2009. Revenues increased from the prior year comparable periods due primarily to higher utilization. For the fourth quarter of 2010 the Contract Drilling Services division achieved a utilization rate, on a spud to release basis, of 58% and a year to date utilization rate of 53%, as compared to 41% and 24% respectively for the same periods in 2009. Operating days (spud to release) for the three and twelve months ended December 31, 2010 totaled 743 days and 2,714 days respectively, as compared to 532 and 1,169 days respectively for the same periods in 2009. Revenue per operating day received for contract drilling services for the three and twelve months ended December 31, 2010 increased by 29% and decreased 3% respectively as compared to the same periods in 2009. The increase in revenue per operating day during the three months ended December 31, 2010 was due primarily to an increase in drilling day rates and the addition of two owned top drives to the fleet in 2010. The decrease in revenue per operating day in 2010 was due primarily to a \$0.9 million payment received in the third quarter of 2009 in consideration of the termination of a one year contract where no such payment was received in 2010.

Rentals and Transportation Services

The revenue reported from Total Energy's Rentals and Transportation Services division increased by 211% to \$36.6 million for the three months ended December 31, 2010 as compared to \$11.8 million for the same period in 2009, and increased by 138% to \$118.3 million for the year ended December 31, 2010 as compared to \$49.6 million for the same period in 2009. Revenue increased from the prior year comparable periods due primarily to the DC Energy acquisition and increased equipment utilization. Average utilization of the rental assets was 69% and 56% respectively for the three and twelve month periods ended December 31, 2010 as compared to 33% and 34% respectively for the

comparable periods in 2009. This division exited the fourth quarter of 2010 with approximately 8,000 pieces of rental equipment, net of certain equipment that was disposed of during the fourth quarter of 2010 due to low utilization, as compared to 4,500 pieces at the end of the fourth quarter of 2009. This division also exited the fourth quarter of 2010 with a fleet of 95 heavy trucks (with an additional 6 trucks added in January 2011) as compared to 74 heavy trucks at the end of the fourth quarter of 2009.

Gas Compression Services

The revenue reported from Total Energy's Gas Compression Services division increased by 175% to \$23.1 million for the three months ended December 31, 2010 as compared to \$8.4 million for the same period in 2009, and increased by 61% to \$62.3 million for the year ended December 31, 2010 as compared to \$38.6 million for the same period in 2009. The revenue variances from the prior year comparable periods were due primarily to increased demand from this division's customers. This division exited the fourth quarter of 2010 with a backlog of fabrication sales orders of approximately \$35.3 million as compared to a backlog of \$11.3 million as at December 31, 2009. As at December 31, 2010 the total horsepower of compressors on lease was approximately 21,200 as compared to approximately 17,600 as at December 31, 2009. The compression rental fleet experienced an average utilization of 73% (based on fleet horsepower) during 2010 as compared to 82% in 2009.

Other

Total Energy's Other division consists of the Company's corporate activities. The Other division does not generate any revenue but provides sales, operating and other support services to Total Energy's operating divisions and wholly owned subsidiaries and partnerships and manages the corporate affairs of the Company.

Operating Expenses

Operating expenses increased 126% to \$40.3 million for the three months ended December 31, 2010 as compared to \$17.8 million for the same period in 2009, and increased by 94% to \$126.9 million for the year ended December 31, 2010 as compared to \$65.5 million for the same period in 2009. The increase resulted primarily from the addition of DC Energy during the first quarter of 2010 and increased costs associated with increased revenues. The gross margin percentage for the three months and year ended December 31, 2010 was 45% and 43% respectively as a percentage of revenue as compared to 35% and 39% respectively for the comparable periods in 2009. A detailed margin analysis for each division is presented in the discussion of Operating Earnings. Operating expenses consist of salaries and benefits for operations personnel, repairs, maintenance, fuel, manufacturing costs and trucking costs.

Selling, General and Administrative Expenses

Selling, general and administrative expenses increased by 75% to \$6.9 million for the three months ended December 31, 2010 as compared to \$4.0 million for the same period in 2009, and increased by 68% to \$25.7 million for the year ended December 31, 2010 as compared to \$15.3 million for the same period in 2009. The increase resulted primarily from the addition of DC Energy during the first quarter of 2010 and increased costs associated with increased revenues.

Included in these costs are compensation for directors and officers pursuant to the Company's cash based compensation plans. Selling, general and administrative expenses also include salaries and benefits for office staff, rent, utilities, and communications in the Company's various divisional offices and its corporate head office as well as professional fees and other costs to maintain the Company's public listing.

Share-based Compensation Expense

Share-based compensation was \$0.4 million and \$1.3 million respectively for the three months and year ended December 31, 2010 versus \$0.3 million and \$1.3 million respectively for the prior year comparable periods. The share-based compensation expense arises from share options granted pursuant to a share option plan implemented during the second quarter of 2009. Additional information with respect to the plan is outlined in Note 15 to the Audited Consolidated Financial Statements.

Depreciation Expense

Depreciation expense increased 52% and 54% respectively for the three and twelve month periods ended December 31, 2010 to \$5.6 million and \$20.4 million respectively, as compared to \$3.7 million and \$13.2 million respectively for the prior year comparable periods. The increase is due primarily to the addition of DC Energy in the first quarter of 2010 and higher equipment utilization in the Contract Drilling Services division. All of the Company's property, plant and equipment is depreciated on a straight-line basis with the exception of contract drilling equipment which is depreciated on a utilization basis.

Other Interest Expense

Other interest expense was \$0.1 million and \$0.2 million respectively for the three and twelve month periods ended December 31, 2010 as compared to \$0.2 million and \$0.6 million respectively for the comparable periods in 2009. The decrease in other interest expense in 2010 was due to reduced operating line of credit balances on the Company's revolving operating facility during 2010. Other interest expense is interest paid on advances under the Company's revolving operating facility.

Interest on Long-term Debt

Interest on long-term debt was \$0.8 million and \$3.1 million respectively for the three and twelve month periods ended December 31, 2010 as compared to \$0.3 million and \$0.9 million respectively for the comparable periods in 2009. The increase in interest on long-term debt during 2010 was due primarily to a higher average loan balance resulting from the DC Energy acquisition and an increase in the effective interest rate on the Company's credit facilities. Included in interest on long-term debt is interest on capital leases.

Operating Earnings

Operating earnings increased 1,555% to \$18.6 million in the fourth quarter of 2010 as compared to \$1.1 million for the comparable period in 2009. For the year ended December 31, 2010 operating earnings increased 352% to \$44.0 million from \$9.7 million for the comparable period in 2009. The increase in operating earnings was due primarily to the addition of DC Energy in the first quarter of 2010 and increased operating earnings in all three business divisions.

The Contract Drilling Services division had operating earnings of \$3.0 million and \$5.2 million respectively for the three months and year ended December 31, 2010, as compared to operating earnings of \$0.5 million and \$1.8 million respectively for the comparable periods in 2009. The operating earnings margin in this division was 23% and 13% respectively for the three months and year ended December 31, 2010 as compared to 6% and 10% respectively for the comparable periods in 2009. The increase in operating earnings margin in 2010 relative to 2009 is due primarily to higher equipment utilization.

The Rentals and Transportation Services division had operating earnings of \$14.7 million and \$38.1 million respectively for the three months and year ended December 31, 2010, as compared to \$1.2 million and \$9.2 million respectively for the comparable periods in 2009. The operating earnings margin in this division was 40% and 32% respectively for the three months and year ended December 31, 2010 as compared to 10% and 18% respectively for the comparable periods in 2009. The 2010 increases in operating earnings margin resulted primarily from higher equipment utilization on operating efficiencies arising from the integration of DC Energy.

The Gas Compression Services division contributed operating earnings of \$2.3 million and \$6.3 million respectively for the three months and year ended December 31, 2010 as compared to \$0.6 million and \$3.1 million for the comparable periods in 2009. The operating earnings margin in this division was 10% for the three months and year ended December 31, 2010 as compared to 7% and 8% respectively for the corresponding periods in 2009. The increase in operating earnings margin resulted primarily from increased sales revenues.

The Other division had operating losses of \$1.4 million and \$5.5 million respectively for the three months and year ended December 31, 2010 as compared to \$1.1 million and \$4.3 million for the corresponding periods in 2009. The increase in operating losses is due primarily to increased compensation expense arising due to increased industry activity and improved financial performance, and the addition of a corporate controller during 2010. The Other division does not include any operational activities relating to Total Energy's business and therefore does not generate any revenue.

Loss on Disposal of Equipment

Loss on disposal of equipment was \$0.7 million and \$0.1 million respectively for the three months and year ended December 31, 2010 as compared to gains of \$0.2 million and \$0.5 million respectively for the comparable periods in 2009. Disposals of equipment result from the replacement and upgrade of older equipment in the Company's fleet as well as the exercise of purchase options on compression equipment previously on lease in the Gas Compression Services division.

Income Taxes and Net Earnings

The Company recorded net earnings of \$16.5 million (\$0.53 per share basic and \$0.52 per share diluted) and net earnings of \$40.0 million (\$1.30 per share basic and \$1.27 per share diluted) respectively for the three months and year ended December 31, 2010 as compared to \$2.1 million (\$0.07 per share basic and diluted) and \$11.6 million (\$0.40 per share basic and diluted) respectively for the corresponding periods in 2009. The Company recorded current income tax expense of \$0.2 for the three months and year ended December 31, 2010 as compared to current income tax expense of \$0.4 million and current income tax recovery of \$2.0 million respectively for the corresponding periods in 2009. The Company recorded future income tax expense of \$1.2 million and \$3.7 million respectively for the three months and year ended December 31, 2010 as compared to future income tax recoveries of \$1.2 million and \$0.3 million respectively for the corresponding periods in 2009. This resulted in an effective tax rate of 9% for the year ended December 31, 2010 versus negative 25% for the prior year comparable period. The increase in the effective tax rate for the year ended December 31, 2010 versus the prior year was due primarily to the recovery of current income taxes in 2009 with no corresponding recovery in 2010, and higher earnings in 2010 as compared to 2009.

Total Energy and one of its non-operating subsidiaries have been re-assessed by the Ontario Ministry of Finance ("Ontario Finance"), Alberta Finance and Enterprise ("Alberta Finance") and the Canada Revenue Agency ("CRA") on account of a corporate re-organization undertaken prior to Total Energy's conversion to a trust in 2005. The Company has received both legal and tax advice indicating that the technical merits of the filings positions taken are strong and, as such, no provisions have been taken with respect to the reassessments. The total amount of the reassessments, including interest, is approximately \$7.3 million, \$8.2 million and \$0.2 million respectively. The Ontario Finance and CRA reassessments represent competing claims on the same underlying taxable income as the Alberta Finance reassessments, such that the Ontario Finance and CRA reassessments cannot be successfully applied with the Alberta Finance reassessments. In addition, the Alberta Finance reassessments include duplicate reassessments on the same underlying taxable income, which duplicate reassessments cannot both be successfully applied. Further, it is the Company's position that the applicable limitation period had expired with respect to a significant portion of the Alberta reassessments making such reassessments invalid. The Company is vigorously defending the filing position taken and has filed notices of objection to the reassessments with the provincial taxation authorities and CRA. These various reassessments relate to approximately \$2.6 million of alleged underlying income taxes owing for the period from 2002 to the conversion of Total Energy to a trust in April 2005.

LIQUIDITY AND CAPITAL RESOURCES

Cash Provided by Operations

Cash provided by operations increased to \$9.6 million and decreased to \$31.0 million respectively for the three months and year ended December 31, 2010 as compared to \$3.9 million and \$32.2 million respectively for the comparable periods in 2009. The increase in cash provided by operations during the three months ended

December 31, 2010 was primarily due to increased operating earnings. The decrease in cash provided by operations during 2010 was due primarily to the timing of the monetization of certain non-cash working capital balances. Cashflow increased for the three months and years ended December 31, 2010 to \$24.4 million and \$65.5 million respectively as compared to \$4.7 million and \$25.4 million for the comparable periods in 2009. The cash flow increases are due primarily to increased operating earnings on account of the DC Energy acquisition and improved industry activity levels. The Company reinvests the remaining cash provided by operations after dividend payments to shareholders into the internal growth of existing businesses, acquisitions, the repayment of long-term debt and obligations under capital leases, or the repurchase of Company shares pursuant to the Company's normal course issuer bid.

Investments

Net cash used in investment activities for the three months and year ended December 31, 2010 was \$8.2 million and \$55.5 million respectively, as compared to \$4.9 million and \$24.4 million for the comparable periods in 2009. The increase in net cash used in investment activities for the year ended December 31, 2010 is due primarily to the DC Energy acquisition. The remaining purchases of property, plant and equipment during 2010 were allocated as follows: \$3.7 million in the Contract Drilling Services division relating primarily to the purchase of rig equipment, \$15.4 million in the Rentals and Transportation Services division relating primarily to new equipment additions and \$8.6 million in the Gas Compression Services division relating primarily to additions to the compression rental fleet. During 2009, the property, plant and equipment additions were as follows: \$5.3 million in the Contract Drilling Services division, \$3.3 million in the Rentals and Transportation Services division and \$10.6 million in the Gas Compression Services division. The purchase of property, plant and equipment during 2010 were offset by proceeds on disposal of property, plant and equipment of \$3.6 million, as compared to \$4.0 million for the comparable period in 2009. The disposals of equipment result from the replacement and upgrade of older equipment in the Company's fleet as well as the exercise of purchase options on compression equipment previously on lease in the Gas Compression Services division.

Financing

For the three months ended December 31, 2010 net cash used in financing activities was \$1.2 million versus net cash provided by financing activities of \$1.0 million for the comparable period in 2009. For the year ended December 31, 2010 net cash provided by financing activities was \$24.7 million versus net cash used in financing activities of \$7.8 million for the comparable period in 2009. The increase in net cash generated in financing activities in 2010 was due primarily to long-term debt advances used to finance the DC Energy acquisition.

Liquidity

The Company had a working capital surplus of \$70.4 million as at December 31, 2010 as compared to \$29.5 million at the end of 2009. This increase in the Company's working capital position is due primarily to increased accounts receivable balances on account of the DC Energy acquisition and increased activity levels in all divisions. As at December 31, 2010 and the date of this MD&A, the Company is in material compliance with all debt covenants and is able to fully utilize all existing credit facilities.

In January 2010 the Company replaced its credit facilities with a \$10 million revolving operating facility and an \$80 million revolving term loan facility. Both facilities were 364 day plus 2 year facilities. In the event of non-renewal of the revolving operating facility, all amounts owing under that facility were due and payable on the two year anniversary following non-renewal. The revolving term loan facility required monthly principal payments in the case of non-renewal, where the outstanding loan balance was amortized over 60 months with 23 equal payments required followed by a final lump sum payment due after 24 months. Performance of the Company of its obligation under the facilities was secured by a first fixed and floating charge on all assets of the Company, its wholly owned subsidiaries and partnerships and certain other collateral security. The rate at which the facilities bear interest was based on a financial ratio with the interest rate ranging from prime plus 1.25% to 2.00%. The replacing of the Company's credit facilities in January 2010 resulted in \$19.9 million of bank indebtedness being reclassified as long-term debt as at December 31, 2009 with the balance of \$8.8 million remaining as current. The renewal date for the facilities was July 12, 2011. In February 2011 these

facilities were replaced by the \$69 million of convertible unsecured subordinated debentures and \$35 million operating facility as outlined below.

On February 9, 2011 the Company issued \$69 million of principal amount convertible unsecured subordinated debentures. The debentures bear interest at 5.75% per annum, with interest payable semi-annually in arrears on March 31 and September 30 and maturing March 31, 2016. Each \$1,000 principal amount of debenture is convertible at the option of the holder at any time prior to the close of business on the earlier of maturity date and the last business day immediately preceding the date fixed for redemption, into 44.6429 common shares of the Company, representing a conversion price of \$22.40, subject to antidilution provisions. Commission to the underwriters and other issuance costs amounted to approximately \$3.0 million. The Company utilized the net proceeds from the offering to repay its existing revolving term bank debt and for general corporate purposes.

On February 17, 2011 the Company secured a \$35 million operating facility with a major Canadian financial institution. The facility is a 2 year committed facility with payments not required until June 2013, assuming non-extension by the lender, bearing interest at prime rate plus 0.50% secured against the Company's cash and cash equivalents, accounts receivable and inventory.

The replacing of the Company's credit facilities in February 2011 resulted in \$6.0 million of debt being reclassified from short-term to long-term as at December 31, 2010. It also resulted in an increase in the Company's available debt facilities from \$90 million to \$104 million with \$72.5 million of long-term debt outstanding as at December 31, 2010.

Dividends and Distributions

For the three months and year ended December 31, 2010 the Company declared dividends of \$1.3 million and \$4.1 million respectively, as compared to dividends of \$0.9 million declared for the three months ended December 31, 2009 and dividends of \$1.7 million and trust distributions of \$3.5 million declared during 2009.

For 2011 the Company expects cash provided by operations, cashflow and net earnings to exceed dividends to shareholders. Management and the board of directors of the Company will monitor the Company's dividend policy with respect to forecasted net earnings, cashflow, cash provided by operations, debt levels, capital expenditures and other investment opportunities and will aim to finance future dividends through cash provided by operations.

SUMMARY OF QUARTERLY RESULTS

(in thousands of dollars except per share amounts)

	Dec. 31, 2010	Financial Quarter Ended (Unaudited)		
		Sept. 30, 2010	Jun 30, 2010	Mar 31, 2010
Revenue	\$ 72,716	\$ 55,237	\$ 35,875	\$ 57,812
Cashflow ⁽¹⁾	24,392	16,110	5,657	19,314
Cash (used in) provided by operations	9,576	(6,004)	16,486	10,957
Net earnings	16,541	9,560	809	13,045
Per share (basic)	0.53	0.31	0.03	0.44
Per share (diluted)	0.52	0.30	0.03	0.43

	Dec 31, 2009	Financial Quarter Ended (Unaudited)		
		Sept 30, 2009	Jun 30, 2009	Mar 31, 2009
Revenue	\$ 27,298	\$ 20,004	\$ 14,722	\$ 44,485
Cashflow ⁽¹⁾	4,702	4,692	3,534	12,438
Cash provided by operations	3,920	808	19,007	8,416
Net earnings (loss)	2,131	2,185	(1,236)	8,560
Per share (basic and diluted)	0.07	0.08	(0.04)	0.29

(1) Refer to "Non-GAAP Measures" for further information

As discussed in 'Seasonality and Cyclicity' above, variations over the quarters are due in part to the cyclical nature of the energy service industry in the WCSB due to the occurrence of "breakup". The first quarter has generally been the strongest quarter for the Company. This strength is due to the northern exposure that the Company has in its Contract Drilling Services and Rentals and Transportation Services divisions. The northern areas are busiest in the winter as these areas are frozen and allow better access to operations locations. The second quarter has generally been the slowest quarter due to "breakup" as described above. Many of the areas that the Company operates in are not accessible during this period when ground conditions do not permit the movement of heavy equipment. The third quarter has generally been the third busiest quarter, as some of the issues associated with "breakup" are no longer affecting access to areas of operations. The fourth quarter has usually been the second busiest quarter of the year as customers are generally able to start accessing northern areas with the onset of winter and the ground freezing. The increase in revenue, cash flow and net earnings for the three months and year ended December 31, 2010 as compared to the comparable periods in 2009 is also due to the DC Energy acquisition and increased activity levels in all divisions.

CONTRACTUAL OBLIGATIONS

At December 31, 2010, the Company had the following contractual obligations:

(in thousands of dollars)	Payments due by year					
	Total	2011	2012	2013	2014	2015 and thereafter
Long-term debt , in case of non-renewal ⁽¹⁾	\$ 72,500	\$ –	\$ –	\$ 3,500	\$ –	\$ 69,000
Commitments ⁽²⁾	7,627	3,373	2,345	930	502	477
Capital leases ⁽³⁾	6,217	3,203	1,687	915	322	90
Purchase obligations ⁽⁴⁾	3,921	3,921	–	–	–	–
Total contractual obligations	\$ 90,265	\$ 10,497	\$ 4,032	\$ 5,345	\$ 824	\$ 69,567

(1) Long-term debt obligations are described in Note 10 to the 2010 Audited Consolidated Financial Statements.

(2) Commitments are described in Note 16 to the 2010 Audited Consolidated Financial Statements.

(3) Capital leases are described in Note 11 to the 2010 Audited Consolidated Financial Statements.

(4) Purchase obligations are described in Note 16 to the 2010 Audited Consolidated Financial Statements and relate to Total Energy's commitment to purchase \$3.9 million of inventory for the Gas Compression Services division.

OFF-BALANCE SHEET ARRANGEMENTS

As at December 31, 2010 and 2009 the Company had no off-balance sheet arrangements.

TRANSACTIONS WITH RELATED PARTIES

During 2010 and the comparable period in 2009 the Company had no material transactions with related parties.

CORPORATE ACQUISITION

On January 15, 2010 the Company completed the acquisition of DC Energy for \$44.2 million. The cash portion of the purchase price of \$31.7 million was financed using the Company's credit facilities and the balance of the purchase price of \$12.5 million was financed through the issuance of an unsecured convertible debenture bearing interest at 5% per annum, maturing on June 30, 2012 and convertible into common shares of the Company at a conversion price of \$7.00 per share. On March 1, 2010 the \$12.5 million convertible debenture was converted into 1,785,715 common shares of the Company.

The assets acquired by the Company as a result of the DC Energy acquisition included approximately 3,600 pieces of rental equipment, 20 heavy trucks and 59 trailers, together with all inventories and other assets (excluding only land and buildings) used in connection with DC Energy's business. The Company also assumed certain leases in respect of real estate and certain vehicles and trailers utilized by DC Energy in the ordinary course of business. The Company recorded a future income tax liability on account of the difference between the accounting value and the tax value of the net assets acquired. The Company is also responsible for up to \$0.9 million of employee retention costs payable over 18 months following completion of the DC Energy acquisition. With the exception of the leases, the future income tax liability and the employee retention costs referenced above, no additional material obligations were assumed by the Company in connection with the acquisition.

CRITICAL ACCOUNTING ESTIMATES

Management is responsible for applying judgment in preparing accounting estimates. Certain estimates and related disclosures included within the financial statements are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from management's current judgments. An accounting estimate is considered critical only if it requires the Company to make assumptions about matters that are highly uncertain at the time the accounting estimate is made, and different estimates the Company could have used would have a material impact on Total Energy's financial condition, changes in financial condition or results of operations.

While there are several estimates and assumptions made by management in the preparation of financial statements in accordance with GAAP, the following critical accounting estimates have been identified by management:

Revenue Recognition

The Company recognizes revenue in its divisions as follows; Contract Drilling Services revenue is recognized when services are provided; Rentals and Transportation Services revenue is recognized when services are provided; and Gas Compression Services revenue is recognized as services are provided or products are sold. The Company's services and products are sold based upon orders or contracts with customers that include fixed or determinable prices based upon daily, hourly, or job rates. Revenue is recognized when services and equipment rentals are provided and when collectability is reasonably assured.

Estimates of Collectibility of Accounts Receivable

The Company has to make an estimate for the collectibility of its accounts receivable. The Company continually reviews its accounts receivable balances and makes an allowance once it considers an accounts receivable balance uncollectible. The actual collectibility of accounts receivable could differ materially from the estimate although management does not consider the risk of a significant loss to be material at this time.

Estimates of Depreciation

Total Energy has significant estimates relating to the depreciation policies for property, plant and equipment. Factors that are included in the estimation include but are not limited to the economic life of the asset and the residual value of the asset at the end of its economic life. The Company makes an estimate based on the best information on these factors that it has at that the time these estimates are performed. Actual results could differ materially if any of these factors are different in the future than the current estimates. See Note 3(b) in the notes to the 2010 Audited Consolidated Financial Statements of the Company for Total Energy's depreciation policy.

Estimates of Tax Pools and Their Recoverability

Total Energy has estimated its tax pools for the income tax provision. The actual tax pools that the Company may be able to use could be materially different in the future. See Note 13 in the 2010 Audited Consolidated Financial Statements of the Company for further information.

Share-based Compensation

Share-based compensation is calculated using the fair value method based upon the Black-Scholes model. In order to establish fair value, estimates and assumptions are used to determine risk-free interest rate, expected term, anticipated volatility, anticipated dividend yield and forfeiture rate. The use of different assumptions could result in different book values for share-based compensation. See Note 15 in the 2010 Audited Consolidated Financial Statements of the Company for further information on the share-based compensation plan.

TRANSITION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS

In 2008 the CICA Accounting Standards Board confirmed its decision requiring all publically accountable entities to report under IFRS with the aim of consistency in the global marketplace. The standards are effective for interim and annual financial statements for fiscal years beginning on or after January 1, 2011. The Company expects the transition will impact accounting, financial reporting, internal controls over financial reporting, taxes, and IT systems and processes. The Company has established an internal IFRS implementation team and has developed an implementation plan as outlined below.

The key elements of Company's changeover plan include:

- determine appropriate changes to accounting policies and required amendments to financial disclosures;
- identify and implement changes in associated processes and information systems;
- comply with internal control requirements; and
- educate and train internal and external stakeholders.

While IFRS uses a conceptual framework similar to Canadian GAAP, there are significant differences on recognition, measurement and disclosures. The Company has completed a review identifying key areas that may be impacted by the transition to IFRS and the areas where there are significant complexities or key decisions required by management prior to the conversion. The Company has determined that four key areas where the change to IFRS may be significant for the Company are with respect to property, plant and equipment, business combinations, revenue and expense recognition and income taxes.

Consistent with Canadian GAAP, under IFRS, property, plant and equipment ("PP&E") are recognized initially at cost. Under International Accounting Standard ("IAS") 16, *Property, Plant and Equipment*, an entity is required to choose, for each class of PP&E, to use either the cost model (consistent with Canadian GAAP) or the revaluation model. Under the revaluation model, an item of PP&E is carried at its revalued amount, being its fair value at the date of the revaluation less any accumulated amortization and accumulated impairment losses. Increases in fair value are recorded in a revaluation surplus account in equity while decreases in fair value serve to reduce the revaluation surplus account, related to the asset, with any excess recognized in income. The Company has elected to use the cost model.

IAS 16, *Property Plant and Equipment* also requires maintaining the book value of property, plant and equipment separately for each significant item even if the combination of those separate items represents one asset for business purposes. The assets have been analyzed and componentized based on significant identifiable components and amortized separately over their respective useful lives. The Company estimates that componentization will result in an approximate \$2.5 million decrease in property, plant and equipment carrying values with a corresponding decrease to retained earnings as at January 1, 2010.

IFRS 3, *Business Combinations*, requires acquisition related costs be expensed in the period in which the costs are incurred and the services received. As a result approximately \$0.6 million of acquisition related costs associated with the DC Energy acquisition that occurred in January 2010 will have to be derecognized and expensed for the comparable three month period ended March 31, 2010. This will reduce the carrying values of property, plant and equipment by approximately \$0.6 million with the corresponding decrease in retained earnings at January 1, 2010.

IAS 11, *Construction Contracts*, provides specific guidance for the recognition of revenues and expenses as it relates to construction contracts. This section requires that revenues and expenses from construction related contracts be

recognized under the percentage of completion method. The Company estimates that transition to the percentage of completion method would result in an approximate \$0.4 million increase in accounts receivable and \$0.04 million decrease in deferred revenue balances, a corresponding \$0.4 million decrease in inventory balances with the net impact of \$0.1 million recognized in retained earnings as at January 1, 2010.

As described in Note 13 to the 2010 Audited Consolidated Financial Statements, the Company recorded a deferred tax credit pursuant to a corporate reorganization undertaken in 2009. IAS 12, *Income Taxes*, does not recognize deferred tax credits. As a result the Company's deferred tax credit balance of \$11.6 million as at January 1, 2010 will be eliminated with a corresponding increase in retained earnings.

IFRS disclosure and presentation requirements are much more extensive than the requirements of Canadian GAAP. The Company's IFRS transition team has developed sample financial statements to enable efficient and timely preparation of the first set of fully compliant IFRS statements for the first quarter 2011.

First Time Adoption of IFRS

Adoption of IFRS requires the application of First-Time Adoption of International Financial Reporting Standards ("IFRS 1") which provides guidance for an entity's initial adoption of IFRS. IFRS 1 lists specific exemptions the Company will use when first adopting IFRS. The most significant exemptions to the Company are as follows:

- **Business combinations**

For business combinations that occurred before the transition date, the Company has the choice to restate all of these business combinations to IFRS standards, restate all business combinations after a particular date, or not to restate any of these business combinations. Assets and liabilities acquired in an un-restated business combination that were recognized under Canadian GAAP and do not qualify for recognition under IFRS are then de-recognized. The Company has elected not to restate business combinations that occurred before the transition date.

- **Fair-value or revaluation as deemed cost**

IFRS required PP&E to be measured at a cost in accordance with IFRS (breaking down material items into components and amortizing each one separately). However, upon transition, IFRS permits an asset to be recognized at deemed cost which is the fair value at the date of transition or an event-driven valuation. The exemption noted above may be applied to individual items of PP&E. Any write-up of the asset to a fair value above cost will be recorded in retained earnings as a revaluation reserve. The Company has elected to measure PP&E at cost as opposed to deemed cost.

- **Information technologies ("IT") and data systems**

Changes in reporting and certain accounting requirements as discussed above will potentially require changes to IT systems or may require the implementation of new ones. Based on the Company's impact assessment significant changes to the Company's IT systems will not be required.

- **Internal controls over financial reporting**

In accordance with Total's approach to the certification of internal controls required under National Instrument 52-109, all entity level, information technology, disclosure and business process controls were reviewed by Total's IFRS transition team. Internal controls under IFRS remain similar to the controls under Canadian GAAP with the exception of management reports that will be redesigned for transition to IFRS.

- Disclosure controls and procedures, including investor relations and external communication plans

A qualitative and quantitative assessment of the impact of the IFRS transition is being communicated in this MD&A. The interim and year end periods of the financial year ending December 31, 2011 will also include comparative information for the interim and year end periods of 2010 prepared under IFRS.

- Financial reporting expertise, including training requirements

The Company believes that it has the necessary IFRS expertise as its IFRS team members have received the training necessary for current and future stages of implementation of IFRS. During the second quarter of 2010 divisional controllers received formal IFRS training to ensure the necessary expertise is present in all levels of financial reporting within the Company.

During the second quarter of 2010, an IFRS information session was held with members of the Board of Directors (including Audit Committee members). During this session management and the Company's external auditors provided the Board with a review of the timeline for implementation, the implications of IFRS standards to the business and an overview of the impact to the financial statements (as experienced in Europe by comparable companies). As a result of the information session, the Audit Committee reviewed the Audit Committee Charter and made necessary changes to reflect the requirements for IFRS financial expertise. The Audit Committee continues to receive and review quarterly IFRS project status updates from management.

- Impact on debt covenants and capital requirements

As described above, it is expected that several transitional adjustments and changes in accounting policies will be made on the transition to IFRS. The transitional adjustments and subsequent accounting for the items described above may result in changes to covenant calculations and will change capital requirements disclosure.

The Company's IFRS transition project is on schedule. The Company's IFRS transition team and management continue to liaise with its external auditors and key stakeholders in the Company to ensure a timely and smooth transition to IFRS in 2011.

FINANCIAL INSTRUMENTS

Risk Management Activities

The Company does not have significant exposure to any individual customer or counter party. No customer accounted for more than 10% of the Company's consolidated revenues during 2010. Concentration of credit risk on the Company's trade accounts receivable exists in the oil and gas industry.

Fair Values

The carrying values of cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities, dividends payable and obligations under capital leases approximate their fair value due to the relatively short periods to maturity of the instruments. Long-term debt utilizes a combination of short term fixed rates through the use of 30 to 90 day Banker's Acceptance and floating rates and accordingly its fair market value approximates its carrying value.

Interest Rate Risk

The Company manages its interest rate risk on borrowings by utilizing a combination of short-term fixed rates through the use of 30 to 90 day Banker's Acceptance rates and floating rates on debt. As at December 31, 2010 virtually all debt was at floating rates.

Foreign Currency Risk

Where foreign currency denominated purchases are made, it is the Company's practice to pay invoiced amounts within 15 days of receipt of invoice to reduce the Company's exposure to foreign exchange risk. In addition, from time to time the Company purchases funds in the foreign currency to which the order is denominated to mitigate against foreign exchange rate changes from the date of ordering to when payment is made. Pricing to customers is also customarily adjusted to reflect changes in the Canadian dollar landed cost of imported goods.

OUTSTANDING COMPANY SHARE DATA

	As at December 31, 2010 (in thousand of shares)
Company Shares	31,425
Share option dilution	<u>671</u>
Diluted Company Shares	<u>32,096</u>

The additional Common Shares are on account of dilutive share options outstanding as at December 31, 2010.

Summary information with respect to share options outstanding is provided below:

<u>Outstanding at December 31, 2010</u>	<u>Exercise Price</u>	<u>Remaining life (years)</u>	<u>Exercisable at December 31, 2010</u>
1,175,000	4.66	3.4	655,000
200,000	4.97	3.8	-
150,000	7.30	4.1	-
<u>50,000</u>	<u>8.54</u>	<u>4.7</u>	<u>10,000</u>
<u>1,575,000</u>	<u>\$5.07</u>	<u>3.6</u>	<u>665,000</u>

On February 9, 2011 the Company issued \$69 million of principal amount unsecured subordinated debentures. The debentures are convertible into 3.1 million common shares with an additional 1.8 million common shares reserved for issuance in connection with the "Change of Control" provision as set out in the trust indenture relating to the debentures.

There has been no change in the number of common shares outstanding from December 31, 2010 to the date of this report.

RISK FACTORS

The following is a summary of certain risk factors relating to the activities of the Company and its subsidiaries.

Risks Relating to the Energy Services Business

General

Certain activities of the Company are affected by factors that are beyond its control or influence. The business and activities of the Company are directly affected by fluctuations in the levels of oil and natural gas exploration, development and production activity carried on by its customers, which, in turn, is dictated by numerous factors, including world energy prices and government policies. Any addition to or elimination or curtailment of government incentives or other material changes to government regulation of the energy industry in Canada could have a significant impact on the oilfield service industry in Canada. While the impact of the global financial crisis and uncertain economic conditions may continue to present a challenging business environment for the Company during 2011, management believes that the Company is reasonably well positioned to operate in such environment.

Industry Conditions

The oil and gas service industry is highly reliant on the levels of capital expenditures made by oil and gas producers and explorers. Exploration and production companies base their capital expenditures on various factors, including but not limited to hydrocarbon prices, exploration and development prospects in various jurisdictions, production levels of their reserves and access to capital. Oil and gas producers and explorers tend to examine long-term fundamentals affecting the foregoing factors before they adjust their capital expenditure plans. Risk factors associated with the Company's operations include business factors and changes in government regulation. Should one or more of these risks materialize, actual results may vary materially from those currently anticipated. In recent years, commodity prices, and therefore, the levels of drilling, production and exploration activity have been volatile. Any prolonged, substantial reduction in commodity prices will likely affect the activity levels of the exploration and production companies and the demand for the Company's products and services. A significant prolonged decline in commodity prices would have a material adverse effect on the Company's business, results of operations and financial condition, including the Company's ability to pay dividends to its Shareholders.

Government Regulation

Total Energy's business and the business of its customers are subject to significant and evolving laws and government regulations, including in the areas of environment, health and safety. Changes to such laws and regulations may impose additional costs on Total Energy and may affect its business in other ways, including the requirement to comply with various operating procedures and guidelines that may impact Total Energy's operations. Total Energy has in place, in each of its divisions, programs for monitoring compliance to ensure that it meets or exceeds applicable laws and regulatory requirements. Ensuring a healthy and safe workplace minimizes injuries and other risks employees may face in carrying out their duties, improves productivity and avoids penalties or other costs and liabilities.

Material changes to the regulations and taxation of the energy industry may reasonably be expected to have an impact on the energy services industry. An increase in royalties or other regulatory burdens would reasonably be expected to result in a material decrease in industry drilling and production activity in the applicable jurisdiction, which in turn would lead to corresponding declines in the demand for the goods and services provided by the Company in such jurisdiction. Conversely, reductions in royalties and other government regulations may reasonably be expected to have a positive impact on Total Energy's business.

Any initiatives by Canada or the provinces in which the Company operates to set legally binding targets to reduce emissions of carbon dioxide, methane, nitrous oxide and other so-called "greenhouse gases" could have direct or indirect compliance costs. Such initiatives and costs may adversely affect the oil and gas business in Canada, which in turn may adversely affect the oil and gas services industry in which the Company participates. The impact of such effects and/or costs is not yet certain.

Credit Risk

A substantial portion of the Company's accounts receivable are with customers involved in the oil and gas industry, whose cash flow may be significantly impacted by many factors including commodity prices, the success of drilling programs, well reservoir decline rates and access to capital. The Company does not have significant exposure to any individual customer or counter-party. No customer accounted for more than 10% of the Company's consolidated revenues during the year ended December 31, 2010. Although collection of these receivables could be influenced by economic factors affecting this industry, management considers the risk of a significant loss to be remote at this time. Management is sensitive to and is continuously monitoring the impact of the global economic and financial crisis on credit risk to the Company.

Currency Fluctuations

The Gas Compression Services division, Bidell, obtains critical components and parts from U.S. suppliers and is therefore subject to foreign exchange rate fluctuations in the procurement of those materials. Where Bidell is contracted to undertake custom work, an exchange rate fluctuation provision is included in the relevant purchase order to reduce Bidell's exposure to such fluctuations. The Company's Contract Drilling Services division and the Rentals and Transportation Services division purchase certain capital equipment from U.S. suppliers and are also subject to foreign exchange rate fluctuations in the procurement of those items. Total Energy has taken measures that it considers reasonable to mitigate its exposure to exchange rate fluctuations, including the purchase of foreign currencies in an amount approximately equal to such foreign currency obligations at any given time. However, there can be no assurance that such measures will reduce Total Energy's exposure to currency fluctuations to a level that is not material.

Competition

The various business segments in which the Company participates are highly competitive. The Company competes with several large national and multinational organizations in the contract drilling services, rental and transportation services and gas compression services businesses. Many of those national and multinational organizations have greater financial and other resources than the Company. There can be no assurance that such competitors will not substantially increase the resources devoted to the development and marketing of products and services that compete with those of the Company or that new competitors will not enter the various markets in which the Company is active. In certain aspects of its business, the Company also competes with a number of small and medium-sized companies, which, like the Company, have certain competitive advantages such as low overhead costs and specialized regional strengths.

Access to Parts, Development of New Technology and Relationships with Key Suppliers

The ability of Bidell to compete and expand is dependent on Bidell having access, at a reasonable cost, to equipment, parts and components, which are at least technologically equivalent to those utilized by competitors and to the development and acquisition of new and competitive technologies. Although Bidell has secured individual distribution agreements with various key suppliers, there can be no assurance that those sources of equipment, parts, components or relationships with key suppliers will be maintained. If these sources and relationships are not maintained, Bidell's ability to compete may be impaired. Bidell is able to access certain distributors and secure discounts on parts and components that would not be available if it were not for its relationship with certain key suppliers. Should the relationships with key suppliers come to an end, the availability and cost of securing certain equipment and parts may be adversely affected. The ability of Chinook to compete and expand is dependent upon Chinook having access, at a reasonable cost, to drilling equipment and supplies that are at least technologically equivalent to those utilized by competitors and to the development and acquisition of new and competitive technologies as industry conditions require. There can be no assurance that existing sources for equipment will be maintained or that new technologically advanced equipment will be acquired. If such equipment is not available, Chinook's ability to compete may be impaired.

Employees

The success of the Company is dependent upon its key personnel. Any loss of the services of such persons could have a material adverse effect on the business and operations of the Company. The ability of the Company to expand its services will be dependent upon its ability to attract additional qualified employees in all of its divisions. The ability to secure the services of additional personnel is constrained in times of strong industry activity. While a modest general economic outlook and slower industry environment has alleviated labour challenges during 2010 relative to past years when activity levels were higher, recent strengthening of industry activity levels in Western Canada is expected to result in a more challenging and competitive labour market.

Environmental Liability Risks

Total Energy routinely deals with natural gas, oil and other petroleum products. The Company has established programs to address compliance with current environmental standards and monitors its practices concerning the handling of environmentally hazardous materials. The Company also generally performs “phase 1” environmental studies on all of its properties prior to acquisition to minimize the risk of acquisition of a contaminated property. However, there can be no assurance that the Company’s procedures will prevent environmental damage occurring from spills of materials handled by the Company or that such damage has not already occurred. As a result of its fabrication and refurbishing operations, Bidell also generates or manages hazardous wastes, such as solvents, thinners, waste paint, waste oil, washdown wastes and sandblast material.

Although the Company attempts to identify and address contamination issues before acquiring properties, and attempts to utilize generally accepted operating and disposal practices, hydrocarbons or other wastes may have been disposed of or released on or under properties owned, leased, operated or worked on by the Company or on or under other locations where such wastes have been taken for disposal. These properties and the wastes disposed thereon may be subject to environmental laws that could require the Company to remove the wastes or remediate sites where they have been released.

Potential Operating Risks and Insurance

Total Energy has an insurance and risk management program in place which has been implemented in an effort to protect its assets, operations and employees. Total Energy also has programs in place to address compliance with current safety and regulatory standards. Total Energy has a health and safety coordinator in each division who is responsible for maintaining and developing policies and monitoring operations vis-à-vis those policies. Third party consultants are also retained as required to assist the divisional health and safety coordinators. Each health and safety coordinator is required to report incidents directly to the Vice President of Operations of Total Energy. However, the Company’s operations are subject to risks inherent in the oil and gas drilling and production services industry, such as equipment defects, malfunction and failures and natural disasters with resultant uncontrollable flows of oil, gas or well fluids, fires, spills and explosions.

These risks could expose the Company to substantial liability for personal injury, loss of life, business interruption, property damage or destruction, pollution and other environmental damages. Although the Company has obtained insurance against certain of the risks to which it is exposed, such insurance is subject to coverage limits and no assurance can be given that such insurance will be adequate to cover the Company’s liabilities or will be generally available in the future or, if available, that premiums will be commercially justifiable. If the Company were to incur substantial liability and such damages were not covered by insurance or were in excess of policy limits, or if the Company were to incur such liability at a time when it is not able to obtain liability insurance, its business, results of operations and financial condition could be materially adversely affected.

Access to Additional Financing

Total Energy may find it necessary in the future to obtain additional debt or equity to support ongoing operations, to undertake capital expenditures or to undertake acquisitions or other business combination transactions. There can be no assurance that additional financing will be available to Total Energy when needed or on terms acceptable to Total Energy, particularly during the current global financial crisis. Total Energy's inability to raise financing to support ongoing operations or to fund capital expenditures or acquisitions could limit the Company's growth and may have a material adverse effect upon the Company.

Seasonality

In general, the level of activity in the Canadian oilfield service industry is influenced by seasonal weather patterns. Wet weather and the spring thaw may make the ground unstable. Consequently, municipalities and provincial transportation departments enforce road bans that restrict the movement of rigs and other heavy equipment, thereby reducing activity levels. Additionally, certain oil and gas producing areas are located in areas that are inaccessible other than during the winter months, because the ground surrounding the drilling sites in these areas consists of swampy terrain. Seasonal factors and unexpected weather patterns may lead to declines in the activity levels of exploration and production companies and corresponding declines in the demand for the goods and services of the Company.

MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL STATEMENTS

The accompanying consolidated financial statements and all information in the Annual Report are the responsibility of management. The consolidated financial statements have been prepared by management in accordance with the accounting policies in the notes to financial statements. When necessary, management has made informed judgments and estimates in accounting for transactions which were not complete at the balance sheet date. In the opinion of management, the financial statements have been prepared within acceptable limits of materiality, and are in accordance with Canadian generally accepted accounting principles (GAAP) appropriate in the circumstances. The financial information elsewhere in the Annual Report has been reviewed to ensure consistency with that in the consolidated financial statements.

Management has prepared Management's Discussion and Analysis (MD&A). The MD&A is based upon Total Energy's financial results prepared in accordance with Canadian GAAP. The MD&A compares the audited financial results for the twelve months ended December 31, 2009 to December 31, 2010.

Management maintains appropriate systems of internal control. Policies and procedures are designed to give reasonable assurance that transactions are properly authorized, assets are safeguarded and financial records properly maintained to provide reliable information for the preparation of financial statements.

KPMG LLP, an independent firm of Chartered Accountants, was engaged, as approved by a vote of shareholders at Total Energy's most recent annual general meeting, to audit the consolidated financial statements in accordance with generally accepted auditing standards in Canada and provide an independent professional opinion.

The Audit Committee of the Board of Directors of Total Energy Services Inc., which is comprised of three independent directors, has discussed the consolidated financial statements, including the notes thereto, with management and external auditors. The consolidated financial statements have been approved by the Board of Directors on the recommendations of the Audit Committee.



DANIEL K. HALYK
President and
Chief Executive Officer

March 10, 2011



MARK A. KEARL, CA
Vice President and
Chief Financial Officer

INDEPENDENT AUDITORS' REPORT

To the Shareholders

Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of Total Energy Services Inc. (the "Company"), which comprise the consolidated balance sheets as at December 31, 2010 and 2009, the consolidated statements of earnings and retained earnings and cash flows for the years then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with Canadian generally accepted accounting principles, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Company as at December 31, 2010 and 2009, and the results of its consolidated operations and its consolidated cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

KPMG LLP

CHARTERED ACCOUNTANTS

Calgary, Canada

March 10, 2011

TOTAL ENERGY SERVICES INC.

Consolidated Balance Sheets

December 31, 2010 and 2009
(in thousands of Canadian dollars)

	2010	2009
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 228	\$ –
Accounts receivable	69,236	22,104
Inventory (note 8)	36,385	28,408
Income taxes receivable	118	2,848
Prepaid expenses and deposits	2,129	2,309
	<u>108,096</u>	<u>55,669</u>
Property, plant and equipment (note 9)	234,448	175,052
Goodwill	4,053	4,053
	<u>\$ 346,597</u>	<u>\$ 234,774</u>
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable and accrued liabilities	\$ 28,285	\$ 12,975
Deferred revenue	4,942	3,001
Dividends payable	1,257	875
Current portion of long-term debt (note 10)	–	8,737
Current portion of obligations under capital leases (note 11)	3,203	588
	<u>37,687</u>	<u>26,176</u>
Long-term debt (note 10)	72,500	34,950
Obligations under capital leases (note 11)	3,014	763
Future income taxes (note 13)	21,811	5,681
Deferred tax credit (note 13)	4,147	11,575
Shareholders' equity:		
Share capital (note 14)	76,268	60,777
Contributed surplus (note 14)	1,769	1,174
Retained earnings	129,401	93,678
	<u>207,438</u>	<u>155,629</u>
Commitments and contingencies (notes 16 & 17)		
Segmented information (note 19)		
Subsequent events (note 20)		
	<u>\$ 346,597</u>	<u>\$ 234,774</u>

See accompanying notes to consolidated financial statements.

Approved by the Board of Total Energy Services Inc.



Director: Greg Melchin



Director: Bruce L. Pachkowski

TOTAL ENERGY SERVICES INC.
Consolidated Statements of Earnings

Years ended December 31, 2010 and 2009
(in thousands of Canadian dollars except per share amounts)

	2010	2009
REVENUE	\$ 221,640	\$ 106,509
Expenses:		
Operating (note 12)	126,902	65,492
Selling, general and administrative	25,698	15,262
Share-based compensation (note 15)	1,289	1,283
Depreciation	20,377	13,211
Other interest	190	599
Interest on long-term debt	3,142	921
	177,598	96,768
Operating earnings:	44,042	9,741
Reorganization costs (note 2)	–	(890)
Gain (loss) on disposal of equipment	(128)	476
Earnings before income taxes	43,914	9,327
Income tax expense (recovery) (note 13):		
Current	235	(2,021)
Future	3,724	(292)
	3,959	(2,313)
Net earnings	\$ 39,955	\$ 11,640
Net Earnings per share (note 14):		
Basic	\$ 1.30	\$ 0.40
Diluted	\$ 1.27	\$ 0.40

See accompanying notes to consolidated financial statements.

TOTAL ENERGY SERVICES INC.
Consolidated Statements of Retained Earnings

Years ended December 31, 2010 and 2009
(in thousands of Canadian dollars)

	2010	2009
Retained earnings, beginning of year	\$ 93,678	\$ 87,349
Net earnings	39,955	11,640
Dividends	(4,050)	(1,748)
Trust distributions	–	(3,486)
Repurchase and cancellation of common shares and trust units in excess of stated capital (note 14)	(182)	(77)
Retained earnings, end of year	<u>\$ 129,401</u>	<u>\$ 93,678</u>

See accompanying notes to consolidated financial statements.

TOTAL ENERGY SERVICES INC.
Consolidated Statements of Cash Flows

Years ended December 31, 2010 and 2009
(in thousands of Canadian dollars)

	2010	2009
Cash provided by (used in):		
Operations:		
Net earnings	\$ 39,955	\$ 11,640
Add (deduct) items not affecting cash:		
Depreciation	20,377	13,211
Share-based compensation	1,289	1,283
Future income taxes (recovery)	3,724	(292)
Loss (gain) on disposal of equipment	128	(476)
	65,473	25,366
Changes in non-cash working capital items (note 18)	(34,458)	6,785
	31,015	32,151
Investing:		
Purchase of property, plant and equipment	(27,690)	(19,212)
DC Energy Services LP acquisition (note 5)	(31,714)	–
Proceeds on disposal of equipment	3,621	3,981
Transaction with Biomerge Industries Ltd. (note 13)	–	(3,639)
Changes in non-cash working capital items	253	(5,522)
	(55,530)	(24,392)
Financing:		
Advances under long-term debt	47,538	31,869
Repayment of long-term debt	(18,725)	(9,703)
Repayment of obligations under capital leases	(2,540)	(172)
Issuance of common shares	2,377	466
Repurchase of common shares	(239)	(131)
Repurchase of trust units	–	(27)
Dividends to Shareholders	(4,050)	(1,748)
Dividends payable	382	875
Distributions to Unitholders	–	(3,486)
Distributions payable	–	(872)
Decrease in bank indebtedness	–	(24,830)
	24,743	(7,759)
Change in cash	228	–
Cash, beginning of year	–	–
Cash, end of year	\$ 228	\$ –
Supplemental cash flow information:		
Interest paid	\$ 3,109	\$ 1,596
Income taxes paid (received)	\$ (2,495)	\$ 3,163

See accompanying notes to consolidated financial statements.

TOTAL ENERGY SERVICES INC.
Notes to the Consolidated Financial Statements

Years ended December 31, 2010 and 2009
(Tabular amounts in thousands of Canadian dollars)

1. Basis of presentation

Total Energy Services Inc. (the “Company”) is incorporated under the Business Corporations Act (Alberta) (the “Act”). The Company was created out of the conversion of Total Energy Services Trust (the “Trust”) to a corporation pursuant to a Plan of Arrangement under the Act, entered into by the Trust, Total Energy Services Ltd. (“TESL”) and Biomerger Industries Ltd. (“Biomerger”) (the “Reorganization”).

Effective upon the closing of the Reorganization on May 20, 2009, the Company became the operator of the business of the Trust and its subsidiaries, and the existing board and management of TESL became the Company’s board and management. The Company did not, as a consequence of the Reorganization, acquire any additional business carried on by Biomerger.

Prior to the Plan of Arrangement effective date of May 20, 2009, the consolidated financial statements include the accounts of the Trust, its subsidiaries and partnership, all of which are wholly owned. After giving effect to the Plan of Arrangement, the consolidated financial statements include the accounts of the Company, its subsidiaries and its partnerships. For financial reporting purposes, the Company is considered a continuing entity of the Trust.

The consolidated financial statements of the Company have been prepared by management in accordance with Canadian generally accepted accounting principles (“GAAP”) and include the accounts of the Company, its subsidiaries and its partnerships. All intercompany balances and transactions have been eliminated.

The Company’s business is the provision of contract drilling services, the rental and transportation of equipment used in oil and natural gas drilling, completion and production processes and the fabrication, sale, rental and servicing of natural gas compression equipment to oil and gas exploration and production companies located primarily in western Canada.

2. Reorganization costs

To effect the conversion to a corporation, the Company incurred \$0.9 million of reorganization costs in 2009. These costs include fees paid to financial, tax and legal advisors, regulatory fees and other costs which have been recognized in the consolidated statement of earnings.

3. Significant accounting policies

(a) Cash and cash equivalents

Cash and cash equivalents consist of cash and short-term investments that are highly liquid in nature and have a maturity date of three months or less.

(b) Property, plant and equipment

Property, plant and equipment are stated at cost. For capital leases, the present value of future minimum lease payments at the inception of the lease is reflected as an asset and a liability on the balance sheet. Depreciation is recorded using the straight-line method over the estimated useful lives of the assets for all assets except contract drilling equipment, which is depreciated using the utilization method. Depreciation rates are as follows:

	Expected life	Residual value	Basis of depreciation
Buildings	20 years	–	straight-line
Furniture and fixtures	5 years	–	straight-line
Shop machinery and equipment	5 years	–	straight-line
Rental equipment	5 to 15 years	25% - 33%	straight-line
Light duty vehicles	3 years	–	straight-line
Heavy duty vehicles	10 years	25%	straight-line
Computer equipment	3 years	–	straight-line
Contract drilling equipment	3,000 operating days	10%	utilization

TOTAL ENERGY SERVICES INC.
Notes to the Consolidated Financial Statements

Years ended December 31, 2010 and 2009
(Tabular amounts in thousands of Canadian dollars)

(c) Inventory and work-in-progress

Parts and raw materials inventory, work-in-progress and finished goods are valued at the lower of cost and net realizable value. Cost for raw materials is determined on a specific item basis, with overhead and labour being determined on a weighted average basis. Cost of work-in-progress and finished goods includes the cost of direct materials, labour and an allocation of manufacturing overhead, all on a specific item basis.

(d) Earnings per share

Basic earnings per share are calculated based on the weighted average number of shares outstanding. Diluted earnings per share includes the weighted average number of shares outstanding plus additional shares from the assumed exercise of in-the-money stock options. The number of additional shares is calculated by assuming proceeds from the exercise of the stock options are used to buy back common shares at the average market price. The additional shares is the difference between the exercised options and the assumed number acquired.

(e) Revenue recognition

The Company recognizes revenue in its segments as follows; Contract Drilling Services revenue is recognized when services are provided; Rentals and Transportation revenue is recognized when services are provided; and Gas Compression Services revenue is recognized as services are provided or products are sold. The Company's services and products are sold based upon orders or contracts with customers that include fixed or determinable prices based upon daily, hourly or job rates. Revenue is recognized when services and equipment rentals are provided and when collectability is reasonably assured.

(f) Transaction costs

Transaction costs are frequently attributed to the issue of a financial asset or liability. The Company has selected a policy of netting all transaction costs with the related financial assets and liabilities.

(g) Measurement of uncertainty

The preparation of the Company's consolidated financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as at the date of the financial statements, as well as the reported amounts for revenue and expenses during the period. Significant estimates and assumptions used in the preparation of the consolidated financial statements include, but are not limited to: estimated useful life, residual values and carrying value of property, plant and equipment; allowance for doubtful accounts; estimated fair value of share based compensation; and, the estimated timing of temporary difference reversals in the calculation of future income taxes and the realization of future income tax assets. Actual results could differ from these estimates.

(h) Income taxes

The Company follows the asset and liability method of accounting for future income taxes. Under the asset and liability method, future income tax assets and liabilities are determined based on "temporary differences" (differences between the accounting basis and the tax basis of the assets and liabilities), and are measured using the currently enacted, or substantively enacted, tax rates and laws expected to apply when these differences reverse. Income tax expense is the sum of the Company's provision for current income taxes and the difference between the opening and ending balances of the future income tax assets and liabilities excluding differences resulting from business combinations and other capital transactions.

TOTAL ENERGY SERVICES INC.
Notes to the Consolidated Financial Statements

Years ended December 31, 2010 and 2009
(Tabular amounts in thousands of Canadian dollars)

(i) Goodwill

Goodwill is the residual amount that results when the purchase price of an acquired business exceeds the sum of the amounts allocated to the assets acquired, less liabilities assumed, based on the fair values. Goodwill is not amortized and is tested for impairment annually in the fourth quarter, or more frequently if events or changes in circumstances indicate that the asset might be impaired. The impairment test is carried out in two steps. In the first step, the carrying amount of the reporting segment is compared to its fair value. When the fair value of the reporting segment exceeds its carrying amount, goodwill of the reporting segment is considered not to be impaired and the second step of the impairment test is unnecessary. The second step is carried out when the carrying amount of the reporting segment's goodwill exceeds its fair value, in which case the implied fair value of the reporting segment's goodwill is compared with its carrying amount to measure the amount of the impairment loss, if any. The implied fair value of goodwill is determined in the same manner as the value of the goodwill in a business combination described above, using the fair value of the goodwill, an impairment loss is recognized in an amount equal to the excess.

(j) Long lived assets

On a periodic basis, management assesses the carrying value of long lived assets for indications of impairment. Indications of impairment include items such as an ongoing lack of profitability and significant changes in technology. When an indication of impairment is present, the Company tests for impairment by comparing the carrying value of the asset to its net recoverable amount. If the carrying amount is greater than the net recoverable amount, the asset is written down to its estimated fair value.

(k) Share-based compensation

The Company has a share option plan as described in note 15. The related share-based compensation expense is recorded for share options issued to employees and non-employees using the fair value method. The fair value of employee share options is valued on the date of grant and the resulting fair value is recorded as an expense over the vesting period of the option. The fair value of non-employee share options are revalued each reporting date with the change in fair value on the vested options recorded in the income statement, and the change in fair value on unvested options expensed over the remaining vesting period. When share based compensation is recorded in the income statement a corresponding credit is recorded in Contributed surplus in Shareholders' equity. When share options are exercised the proceeds received net of any directly attributable transactions costs are credited to share capital and the share-based compensation transferred from Contributed surplus. To date, share options have only been issued to employees of the Company.

In determining the fair value of the share options granted, the Black-Scholes model is used and assumptions regarding interest rates, underlying volatility of the Company's shares, dividend yields, forfeitures and expected life of the options are made.

(l) Comparative amounts

Certain prior-period balances have been reclassified to conform to the current period's presentation.

4. Recent Canadian Accounting Pronouncements Not Yet Adopted

In 2008 the CICA Accounting Standards Board confirmed its decision requiring all publically accountable entities to report under International Financial Reporting Standards ("IFRS") with the aim of consistency in the global marketplace. The standards are effective for interim and annual financial statements for fiscal years beginning on or after January 1, 2011.

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5. DC Energy Services Limited Partnership acquisition

The Company completed the acquisition of the oilfield service, rental and transportation business of DC Energy Services Limited Partnership (“DC Energy”) on January 15, 2010. The cash portion of the purchase price was financed using the Company’s credit facilities (see note 10) and the balance of the purchase price was financed through the issuance of an unsecured convertible debenture bearing interest at 5% per annum, maturing on June 30, 2012 and convertible into common shares of the Company at a conversion price of \$7.00 per share. On March 1, 2010 the convertible debenture was converted into 1,785,715 common shares of the Company.

The acquisition was accounted for as a business combination using the purchase method of accounting and the operations of DC Energy were included in the Company’s accounts effective January 15, 2010. The following table details the purchase price allocation for the business combination:

Net assets acquired:

Property, plant and equipment	\$ 52,002
Inventory	766
Other assets	100
Obligations under capital leases	(3,676)
Future income tax liability	<u>(4,978)</u>
Total	<u>\$ 44,214</u>

Consideration paid:

Cash	\$ 31,888
Convertible debentures	12,500
Net earnings from effective date of sale to closing date of sale	(795)
Transaction costs	<u>621</u>
Total	<u>\$ 44,214</u>

With the exception of certain leases in respect of real estate, the obligations under capital leases and future income tax liability referenced above, and up to \$0.9 million of employee retention costs payable prior to August 2011, no additional material obligations were acquired by the Company in the transaction.

6. Capital management

The Company’s capital management strategy is to maintain a strong capital base in order to maintain investor, creditor and market confidence and to sustain the future development of the Company’s business.

The Company manages its capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the Company’s underlying businesses. The Company seeks to maintain an appropriate balance between the level of long-term debt and shareholders’ equity to ensure access to the capital markets to fund growth and working capital having regard to the cyclical nature of the oilfield services industry. Historically the Company has maintained a conservative ratio of long-term debt to long-term debt plus equity. As at December 31, 2010 and 2009 these ratios were as follows:

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	2010	2009
Long-term debt (including current portion)	\$ 72,500	\$ 43,687
Shareholders' equity	207,438	155,629
Total capitalization	\$ 279,938	\$ 199,316
Long-term debt to long-term debt plus equity ratio	0.26	0.22

As at December 31, 2010 the Company was subject to externally imposed minimum capital requirements relating to its credit facilities. These minimum capital requirements included meeting certain minimum pre-determined ratios with respect to current assets and liabilities, debt and earnings (subject to adjustments), debt and capitalization, fixed charge coverage and margin requirements with respect to both current assets and capital assets. Increases to the Company's quarterly dividend also required the prior written consent of the Company's lenders. The Company monitored these requirements to ensure compliance with them. As at December 31, 2010, the Company was in compliance with all external minimum capital requirements.

7. Financial instruments

A financial instrument is any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument to another entity. Upon initial recognition all financial instruments, including derivatives, are recognized on the balance sheet at fair value. Subsequent measurement is then based on the financial instruments being classified into one of five categories: held for trading, held to maturity, loans and receivables, available for sale and other liabilities. The Company has designated its financial instruments into the following categories applying the indicated measurement methods:

Financial Instrument	Category	Measurement Method
Cash and cash equivalents	Held for trading	Fair value
Accounts receivable	Loans and receivables	Amortized cost
Accounts payable and accrued liabilities	Other liabilities	Amortized cost
Dividends payable	Other liabilities	Amortized cost
Capital leases	Other liabilities	Amortized cost
Long-term debt	Other liabilities	Amortized cost

The Company's financial instruments as at December 31, 2010 include cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities, dividends payable, obligations under capital leases and long-term debt. The fair value of cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities, dividends payable and obligations under capital leases approximate their carrying amounts due to their short-terms to maturity. Long-term debt utilizes a combination of short term fixed rates through the use of 30 to 90 day Banker's Acceptance and floating rates and accordingly its fair market value approximates the carrying value.

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The following maturity analysis shows the remaining contractual maturities for the Company's financial liabilities:

	2011	2012	2013	2014	2015	Thereafter	Total
Accounts payable and accrued liabilities	\$ 28,285	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 28,285
Dividends payable	1,257	-	-	-	-	-	1,257
Long-term debt	-	-	3,500	-	-	69,000	72,500
Capital leases	3,203	1,687	915	322	90	-	6,217
Total	\$ 32,745	\$ 1,687	\$ 4,415	\$ 322	\$ 90	\$ 69,000	\$ 108,259

The Company has exposure to the following risks from its use of financial instruments:

- Credit risk
- Liquidity risk
- Market risk

This note presents information about the Company's exposure to each of the above risks and the Company's objectives, policies and processes for measuring and managing risk. Further quantitative disclosures are included throughout these financial statements.

Credit risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Company's trade accounts receivable. The carrying amount of cash and cash equivalents and accounts receivable included on the balance sheet represent the maximum credit exposure.

The vast majority of the Company's trade accounts receivable are customers involved in the oil and gas industry, and the ultimate collection of the accounts receivable is dependent on both industry related factors and customer specific factors. Industry related factors that may affect collection include commodity prices and access to capital. Customer specific factors that may effect collection include realized commodity prices, the success of drilling programs, well reservoir decline rates and access to capital. As at December 31, 2010, \$ 4.1 million, or 6% of accounts receivable (2009 - \$1.7 million or 7%) were more than 90 days overdue, which is in the range of historical aging profiles. The movement in the Company's allowance for doubtful accounts for 2010 was as follows:

	Allowance for doubtful accounts
Balance at January 1, 2010	\$ 1,198
Provisions and revisions	88
Balance at December 31, 2010	<u>\$ 1,286</u>

The Company does not have significant exposure to any individual customer or counter party. No customer accounted for more than 10% of the Company's consolidated revenues during the year ended December 31, 2010. Concentration of credit risk on the Company's trade accounts receivable exists in the oil and gas industry.

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Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they are due. The Company's approach to managing liquidity is to ensure, to the extent reasonably possible, that it will have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions without incurring unacceptable costs or losses or risking harm to the Company's reputation. As at December 31, 2010 the Company maintained an operating line of credit and long-term debt facility which were available to a maximum of \$90 million to ensure the Company has sufficient working capital to operate its business. As at December 31, 2010 approximately \$17.5 million of these facilities remained unutilized.

In February 2011 the Company replaced its existing credit facilities with \$69 million of principal amount convertible unsecured subordinated debentures and a \$35 million operating facility with a major Canadian financial institution (see note 20).

The Company expects that cash flow from operations, together with existing and available credit facilities, will be sufficient to fund its presently anticipated requirements for investments in working capital, capital assets, dividend payments and the Company's share repurchases.

Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates and interest rates will affect the Company's net earnings or the value of its financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable limits, while maximizing returns.

- Foreign currency exchange rate risk

Foreign currency exchange rate risk is the risk that the fair value of future cash flows will fluctuate as a result of changes in foreign exchange rates. Currently all of the Company's sales are denominated in Canadian dollars, which is the Company's functional currency, and as such the Company does not have any foreign currency exchange rate risk with respect to revenues. The Company estimates that less than 20% of its operating expenses in 2010 were purchased using a foreign currency. Where foreign currency denominated purchases are made, it is the Company's practice to pay invoiced amounts within 15 days of receipt of invoice to reduce the Company's exposure to foreign exchange risk. In addition, from time to time the Company purchases funds in the foreign currency to which the order is denominated to mitigate against foreign exchange rate changes from the date of ordering to when payment is made. Pricing to customers is also customarily adjusted to reflect changes in the Canadian dollar landed cost of imported goods.

The Company had no foreign exchange derivative contracts in place as at or during the year ended December 31, 2010.

- Interest rate risk

Interest rate risk is the risk that future cash flows will fluctuate as a result of changes in market interest rates. The Company is exposed to interest rate fluctuations on its borrowings which utilize a combination of short term fixed rates through the use of 30 to 90 day Banker's Acceptance and floating rates. For the year ending December 31, 2010, if interest rates had been 1% lower with all other variables held constant, after tax net earnings for the period would have been approximately \$445,000 higher (2009 - \$327,000), due to lower interest expense. An equal and opposite impact would have occurred to net earnings had interest rates been 1% higher. The sensitivity is higher in 2010 as compared to 2009 due primarily to higher average loan balances.

The Company had no interest rate swap or financial contracts in place as at or during the year ended December 31, 2010.

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8. Inventory

	2010	2009
Finished goods	\$ 6,185	\$ 7,121
Work-in-progress	8,637	2,835
Parts and raw materials	21,563	18,452
	<u>\$ 36,385</u>	<u>\$ 28,408</u>

9. Property, plant and equipment

December 31, 2010	Cost	Accumulated depreciation	Net book value
Land and buildings	\$ 15,754	\$ 3,324	\$ 12,430
Office and computer equipment	3,736	2,897	839
Shop machinery and equipment	3,588	2,049	1,539
Rental equipment	165,360	41,456	123,904
Automotive equipment	40,336	14,706	25,630
Automotive equipment under capital leases	9,125	2,074	7,051
Contract drilling equipment	88,677	25,660	63,017
Other	400	362	38
	<u>\$ 326,976</u>	<u>\$ 92,528</u>	<u>\$ 234,448</u>

December 31, 2009	Cost	Accumulated depreciation	Net book value
Land and buildings	\$ 10,158	\$ 2,777	\$ 7,381
Office and computer equipment	3,143	2,529	614
Shop machinery and equipment	2,186	1,789	397
Rental equipment	111,282	33,264	78,018
Automotive equipment	35,171	12,683	22,488
Automotive equipment under capital leases	1,777	462	1,315
Contract drilling equipment	85,029	20,293	64,736
Other	400	297	103
	<u>\$ 249,146</u>	<u>\$ 74,094</u>	<u>\$ 175,052</u>

10. Long-term debt

In 2009 the Company had an operating line of credit that was payable on demand. The maximum available under the facility was \$30 million. The facility was secured by a first fixed and floating charge on all assets of the Company, Bidell LP and certain other collateral security and bore interest at the bank's prime rate plus 1.25%.

In 2009 the Company also had a long-term debt facility with each drawdown repaid over sixty months and was available to a maximum of \$35 million. The facility was secured by a first fixed and floating charge on all assets of the Company, Bidell LP and certain other collateral security and bore interest at the bank's prime rate plus 1.50%.

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In January 2010 the Company replaced its credit facilities with a \$10 million revolving operating facility and an \$80 million revolving term loan facility. Both facilities were 364 day plus 2 year facilities. In the event of non-renewal of the revolving operating facility, all amounts owing under that facility were due and payable on the two year anniversary following non-renewal. The revolving term loan facility required monthly principal payments in the case of non-renewal, where the outstanding loan balance was amortized over 60 months with 23 equal payments required followed by a final lump sum payment due after 24 months. The Company's obligation under the facilities was secured by a first fixed and floating charge on all assets of the Company, its wholly owned subsidiaries and partnerships and certain other collateral security. The rate at which the facilities bear interest was based on a financial ratio with the interest rate ranging from prime plus 1.25% to 2.00%. The replacing of the Company's credit facilities in January 2010 resulted in \$19.9 million of bank indebtedness being reclassified as long-term debt as at December 31, 2009 with the balance of \$8.8 million remaining as current. The renewal date for the facilities was July 12, 2011. In February 2011 these facilities were replaced by the \$69 million of convertible unsecured subordinated debentures and \$35 million operating facility as outlined below.

On February 9, 2011 the Company issued \$69 million of principal amount convertible unsecured subordinated debentures. The debentures bear interest from the date of issue at 5.75% per annum, with interest payable semi-annually in arrears on March 31 and September 30 and maturing March 31, 2016. Commission to the underwriters and other issuance costs amounted to approximately \$3.0 million (see note 20).

On February 17, 2011 the Company secured a \$35 million operating facility with a major Canadian financial institution. The facility is a 2 year committed facility with payments not required until June 2013, assuming non-extension by the lender, bearing interest at prime rate plus 0.50% secured against the Company's cash and cash equivalents, accounts receivable and inventory (see note 20).

The replacing of the Company's credit facilities in February 2011 resulted in \$6.0 million of debt being reclassified from short-term to long-term as at December 31, 2010.

	2010	2009
Long-term debt	\$ 72,500	\$ 43,687
Less current portion	-	8,737
Balance, December 31	<u>\$ 72,500</u>	<u>\$ 34,950</u>

Principal payments over the next 5 years are due as follows based on the convertible debenture issuance and recently completed credit facility in February 2011, assuming non-renewal of the credit facility and non-conversion of the convertible debentures:

2011	\$ -
2012	-
2013	3,500
2014	-
2015	-
2016	<u>69,000</u>
Total	<u>\$ 72,500</u>

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11. Obligations under capital leases

	2010	2009
Equipment under capital lease	\$ 6,217	\$ 1,351
Less current portion	<u>3,203</u>	<u>588</u>
Balance, December 31	<u>\$ 3,014</u>	<u>\$ 763</u>

The Company has entered into various agreements with third parties for the purpose of financing certain automotive equipment. The leases bear interest at rates ranging from 2.75% - 5.25% and mature on various dates up to 2015 (see note 7).

In 2010, interest of \$0.3 million (2009 - \$45,000) relating to capital lease obligations has been included in interest on long-term debt.

12. Operating expenses

The amount of inventory recognized as an expense and included in operating expenses during the year ended December 31, 2010 was \$41.8 million (2009 - \$25.2 million) in respect of the Gas Compression Services Division.

13. Income taxes

On May 20, 2009 the Company converted from a trust to a corporation by way of a Plan of Arrangement with TESL and Biomerge. Biomerge had non-capital losses which are available to reduce the future taxable income of the Company in the amount of approximately \$51.7 million. Biomerge also had research and development expenditures which are available to reduce the future taxable income of the Company in the amount of approximately \$23.2 million which have an unlimited carry-forward period. A future income tax asset of \$20.4 million was recognized on conversion with respect to these amounts and was recorded as a reduction to the Company's future income tax liability. The fair value paid for Biomerge was \$3.9 million of which \$3.6 million was paid in cash and the balance was paid through the issuance of 56,730 common shares of the Company. The difference between the future income tax asset recognized and the fair value of the tax pools was recorded as a deferred tax credit in the amount of \$16.5 million on conversion. The balance was subsequently reduced by \$12.4 million on the application of tax pools utilized during 2009 and 2010. Biomerge also had investment tax credits and capital losses totaling approximately \$3 million. Due to their limited use the benefits of these non-refundable investment tax credits and capital losses have not been recognized in these financial statements.

The Company estimates that the remaining non-capital losses will be fully utilized in 2010, along with approximately \$4.0 million of the research and development expenditures. As a result approximately \$19.2 million of research and development expenditures, which have an unlimited carry-forward period, will be available for use in 2011 and future periods.

Income tax expense differs from the amount that would be computed by applying the Federal and Provincial statutory income tax rates. The reasons for the differences are as follows:

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	2010	2009
Income tax rate	28.00%	29.00%
Expected tax expense	\$ 12,296	\$ 2,705
Decrease in taxes resulting from:		
Drawdown of deferred tax credit	(7,428)	(4,932)
Amounts included in trust income	-	(1,052)
Non-deductible share-based compensation	361	372
Future income tax rate adjustment	(1,192)	236
Other	(78)	358
Provision for (recovery of) income taxes	<u>\$ 3,959</u>	<u>\$ (2,313)</u>

The components of the net future income tax liability at December 31 are as follows:

	2010	2009
Future income tax assets:		
Non capital loss and SR&ED carryforward	<u>\$ 10,163</u>	<u>\$ 18,706</u>
Future income tax liabilities:		
Property, plant and equipment	31,860	24,325
Other	114	62
	<u>31,974</u>	<u>24,387</u>
Net future income tax liabilities	<u>\$ 21,811</u>	<u>\$ 5,681</u>

The future income tax asset is comprised of approximately \$20.0 million of non-capital losses (2009 - \$51.7 million) and \$19.2 million of research and development expenditures (2009 - \$23.2 million). The non-capital losses expire in 2029 if not utilized. The research and development expenditures have an unlimited carry-forward period.

The business and operations of the Company are complex and the Company has executed a number of significant financings, reorganizations, acquisitions and other material transactions over the course of its history. The computation of income taxes payable as a result of these transactions involves many complex factors as well as the Company's interpretation of relevant tax legislation and regulations. The Company's management believes that the provision for income tax is adequate and in accordance with generally accepted accounting principles and applicable legislation and regulations. However, tax filing positions are subject to review by taxation authorities who may successfully challenge the Company's interpretation of the applicable tax legislation and regulations.

14. Share Capital

Pursuant to the terms of the Plan of Arrangement, the Company acquired and cancelled all of the issued and outstanding trust units on May 20, 2009. Each Trust unit holder, in exchange for one trust unit, received one common share of the Company. Securityholders of Biomerge received a combination of cash and common shares of the Company in exchange for their securities of Biomerge. Prior to the exchange, the Trust had 29,050,000 trust units outstanding, and immediately subsequent to the exchange, there were 29,106,730 common shares outstanding.

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(a) Trust unit capital:

Trust Units of Total Energy Services Trust	Number of Units (in thousands)	Amount
Balance, December 31, 2008	29,057	\$ 60,027
Repurchased and cancelled	(7)	(15)
Balance, May 19, 2009	29,050	60,012
Decrease resulting from implementation of Plan Arrangement	(29,050)	(60,012)
Balance, December 31, 2009 and 2010	—	\$ —

During 2009 and prior to the Company's conversion from a trust to a corporation 6,900 Trust Units were purchased under the Trust's normal course issuer bid at an average of \$3.97 per Unit, including commissions, and these Units were cancelled. The excess of the price paid over the average price per Trust Unit has been charged to retained earnings.

(b) Common share capital

Common shares of Total Energy Services Inc.

(i) Authorized:

Unlimited number of common voting shares, without nominal or par value.

Unlimited number of preferred shares.

(ii) Common shares issued:

	Number of Shares (in thousands)	Amount
Balance, May 19, 2009	—	\$ —
Issued to Trust unitholders pursuant to Plan of Arrangement	29,050	60,012
Issued to Biomerge securityholders pursuant to Plan of Arrangement	57	256
Repurchased and cancelled	(31)	(66)
Issued on exercise of share options	100	575
Balance, December 31, 2009	29,176	60,777
Issued on conversion of convertible debenture (see note 5)	1,786	12,500
Issued on exercise of share options	495	3,071
Repurchased and cancelled	(27)	(68)
Cancelled	(5)	(12)
Balance, December 31, 2010	31,425	\$ 76,268

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During 2010 27,115 (2009 – 30,330) Common Shares were purchased under the Company's normal course issuer bid at an average price of \$8.80 (2009 - \$4.30), including commissions, and these Common Shares were cancelled. The excess of the price paid over the average price per Common share has been charged to retained earnings. In addition, 5,000 Common Shares were purchased in 2009 pursuant to an employee retention plan at a price of \$4.60, including commissions. These shares were cancelled in 2010 as such shares did not vest pursuant to such retention plan.

(c) Per Share amounts:

Basic and diluted earnings per share for 2010 and 2009 has been calculated on the basis of the weighted average number of common shares outstanding as outlined below:

	Year Ended December 31, 2010	Year Ended December 31, 2009
Weighted average number of shares outstanding - Basic	30,771	29,099
Share option dilution	671	–
Weighted average number of shares outstanding - Diluted	31,442	29,099

Earnings per share for 2009 have been calculated assuming common shares had been outstanding throughout 2009.

Share option dilution for 2010 excludes 50,000 share options (2009 – 1,960,000 share options) that were anti dilutive for the year then ended.

(d) Contributed surplus:

Balance, January 1, 2009	\$	–
Non-cash compensation expense related to share based compensation plan		1,283
Less: Contributed surplus on share options exercised		(109)
Balance, December 31, 2009	\$	1,174
Non-cash compensation expense related to share based compensation plan		1,289
Less: Contributed surplus on share options exercised		(694)
Balance, December 31, 2010	\$	1,769

15. Share-Based Compensation Plan

On June 1, 2009 the Company implemented a share option plan (the "TSX Plan") which was drafted to comply with the policies of the Toronto Stock Exchange. Under the TSX Plan, options to acquire common shares of the Company may be granted to officers and employees of the Company and to consultants retained by the Company.

The aggregate number of common shares issuable upon the exercise of options outstanding under the TSX Plan at any time may not exceed 10% of the issued and outstanding common shares and the aggregate number of common shares issuable to any one officer, director or full time employee of the Company may not exceed 5% of the total number of issued and outstanding common shares. The period to which an option granted under the TSX Plan is exercisable may not exceed ten years from the date such option is granted. The price at which common shares may be acquired upon the exercise of an option is determined with reference to the weighted average closing price of the common shares the five business days immediately prior to the date of grant on which a board lot of common shares trades on the Toronto Stock Exchange.

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Share option transactions during 2010 and 2009 were as follows:

	Weighted average exercise price	Number of Options
Balance, January 1, 2009	\$ -	-
Granted	\$ 4.70	2,160,000
Forfeited	\$ 4.66	(200,000)
Exercised	\$ 4.66	(100,000)
Balance, December 31, 2009	\$ 4.71	1,860,000
Granted	\$ 7.65	210,000
Exercised	\$ 4.80	(495,000)
Balance, December 31, 2010	\$ 5.07	1,575,000

The options issued under the TSX Plan vest either 1/3 on the date of grant, 1/3 after one year and 1/3 after two years or 1/3 on the first anniversary from the date of grant, 1/3 after two years and 1/3 after three years. The options expire on various dates ranging from May 31, 2014 to August 12, 2015.

Summary information with respect to share options outstanding is provided below:

Outstanding at December 31, 2010	Exercise Price	Remaining life (years)	Exercisable at December 31, 2010
1,175,000	4.66	3.4	655,000
200,000	4.97	3.8	-
150,000	7.30	4.1	-
50,000	8.54	4.7	10,000
1,575,000	\$5.07	3.6	665,000

The Company uses the Black-Scholes option-pricing model to determine the estimated fair value of the share options granted. The average per share fair value of the options granted during 2010 is \$2.61 per option (2009 - \$1.41) using the following assumptions:

	2010	2009
Expected volatility	47% to 54%	45% to 54%
Annual dividend yield	1.4% to 1.6%	2.4% to 2.6%
Risk free interest rate	1.4% to 2.4%	1.25% to 2.6%
Forfeitures	15%	15%
Expected life (years)	2 to 5 years	2 to 5 years

For the year ended December 31, 2010 the Company recognized share based compensation expense of \$1.3 million (2009 - \$1.3 million).

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16. Commitments

The Company has operating lease commitments for vehicles and buildings over the next five years as follows:

2011	\$	3,373
2012		2,345
2013		930
2014		502
2015 and thereafter		477

The Company also has purchase obligations of \$3.9 million as at December 31, 2010 relating to commitments to acquire inventory.

17. Contingencies

TESL and one of its non-operating subsidiaries have been re-assessed by the Ontario Ministry of Finance (“Ontario Finance”), Alberta Finance and Enterprise (“Alberta Finance”) and the Canada Revenue Agency (“CRA”) on account of a corporate re-organization undertaken prior to TESL’s conversion to a trust in 2005. The Company has received both legal and tax advice indicating that the technical merits of the filings positions taken are strong and, as such, no provisions have been taken with respect to the reassessments. The total amount of each of the three reassessments, including interest, is approximately \$7.3 million, \$8.2 million and \$0.2 million respectively. The Ontario Finance and CRA reassessments represent competing claims on the same underlying taxable income as the Alberta Finance reassessments, such that the Ontario Finance and CRA reassessments cannot be successfully applied with the Alberta Finance reassessments. In addition, the Alberta Finance reassessments include duplicate reassessments on the same underlying taxable income, which duplicate reassessments cannot both be successfully applied. Further, it is the Company’s position that the applicable limitation period has expired with respect to a significant portion of the Alberta reassessments making such reassessments invalid. The Company is vigorously defending the filing position taken and has filed notices of objection to the reassessments with the appropriate taxation authorities. These various reassessments relate to approximately \$2.6 million of alleged underlying income taxes owing for the period from 2002 to the trust conversion in April 2005.

The Company, in the normal course of operations, will become subject to a variety of legal and other claims against the Company. Management and the Company’s legal counsel evaluate all claims on their apparent merits, and accrue management’s best estimate of the estimated costs to satisfy such claims. Management believes that the outcome of legal and other claims filed against the Company will not be material to the Company.

18. Changes in non-cash working capital items

	2010	2009
Accounts receivable	\$ (47,132)	\$ 15,170
Inventory	(7,211)	5,428
Income taxes receivable	2,730	(2,848)
Prepaid expenses and deposits	157	(990)
Accounts payable and accrued liabilities	15,057	(4,401)
Deferred revenue	1,941	(3,238)
Income taxes payable	–	(2,336)
	<u>\$ (34,458)</u>	<u>\$ 6,785</u>

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19. Segmented information

The Company operates in three main industry segments which are substantially in one geographic segment. These segments are Contract Drilling Services, which includes the contracting of drilling equipment and the provision of labour required to operate the equipment, Rentals and Transportation Services, which includes the rental and transportation of equipment used in oil and natural gas drilling, completion and production operations and Gas Compression Services, which includes the fabrication, sale, rental and servicing of natural gas compression equipment.

The segmented amounts are as follows:

As at and for the twelve months ended December 31, 2010	Contract Drilling Services	Rentals and Transportation Services	Gas Compression Services	Other ⁽³⁾	Total
Revenue	\$ 41,127	\$ 118,259	\$ 62,254	\$ –	\$ 221,640
Operating earnings ⁽¹⁾	5,219	38,066	6,253	(5,496)	44,042
Depreciation	5,574	12,819	1,954	30	20,377
Assets	80,001	188,961	74,413	3,222	346,597
Goodwill	–	2,514	1,539	–	4,053
Capital expenditures ⁽²⁾	3,656	15,412	8,592	30	27,690

As at and for the twelve months ended December 31, 2009	Contract Drilling Services	Rentals and Transportation Services	Gas Compression Services	Other ⁽³⁾	Total
Revenue	\$ 18,304	\$ 49,624	\$ 38,581	\$ –	\$ 106,509
Operating earnings ⁽¹⁾	1,809	9,159	3,077	(4,304)	9,741
Depreciation	2,547	9,122	1,515	27	13,211
Assets	72,946	101,060	56,676	4,092	234,774
Goodwill	–	2,514	1,539	–	4,053
Capital expenditures ⁽²⁾	5,333	3,290	10,589	–	19,212

(1) Operating earnings (loss) are earnings before the gain (loss) on disposal of equipment, reorganization costs and income taxes. Included in operating earnings (loss) for each reportable segment is interest expense paid on the Company's credit facilities. This interest is allocated to each reportable segment based on the relative amount of capital each segment employs.

(2) Excludes the acquisition of DC Energy (see note 5).

(3) Other includes the Company's corporate activities.

20. Subsequent event

- (a) In February 2011 the Company's existing credit facilities were replaced by \$69 million of convertible unsecured subordinated debentures and a \$35 million operating facility as described below.
- (b) On February 9, 2011 the Company issued \$69 million of principal amount convertible unsecured subordinated debentures. The debentures bear interest from the date of issue at 5.75% per annum, with interest payable semi-annually in arrears on March 31 and September 30. Commission to the underwriters and other issuance costs amounted to approximately \$3.0 million. The Company utilized the net proceeds from the offering of approximately \$66.0 million to repay the existing revolving term bank debt and for general corporate purposes.

The debentures mature on March 31, 2016. The debentures are not redeemable at the option of the Company on or before March 31, 2014. After March 31, 2014, and on or before March 31, 2015, the debentures may be redeemed

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in whole or in part from time to time at the option of the Company at their principal amount plus accrued and unpaid interest, provided that the weighted average trading price of the Company's common shares on the Toronto Stock Exchange for the 20 consecutive trading days ending five days preceding the date on which the notice of redemption is given is at least 125 per cent of the conversion price. After March 31, 2015 the debentures may be redeemed in whole or in part at the option of the Company at a price equal to their principal amount plus accrued and unpaid interest.

Each \$1,000 principal amount of debentures will be convertible at the option of the holder at any time prior to the close of business on the earlier of (i) the maturity date and (ii) the last business day immediately preceding the date fixed for redemption, into 44.6429 common shares of the Company, representing a conversion price of \$22.40, subject to anti-dilution provisions. Holders who convert their debentures will receive accrued and unpaid interest for the period from the date of the latest interest payment date to the date of the conversion.

- (c) On February 17, 2011 the Company secured a \$35 million operating facility with a major Canadian financial institution. The facility is a 2 year committed facility with payments not required until June 2013, assuming non-extension by the lender, bearing interest at prime rate plus 0.50% secured against the Company's cash and cash equivalents, accounts receivable and inventory.

CORPORATE INFORMATION

BOARD OF DIRECTORS

Bruce Pachkowski ³
Chairman of the Board

Daniel Halyk
President and Chief Executive Officer

Gregory Fletcher ^{1 2}

Randy Kwasnacia ^{1 3}

Greg Melchin ^{1 2}

Andrew Wiswell ^{2 3}

¹ Member of the Compensation Committee

² Member of the Audit Committee

³ Member of the Corporate Governance and Nominating Committee

MANAGEMENT TEAM

TOTAL ENERGY SERVICES INC.

Daniel Halyk
President and Chief Executive Officer

Brad Macson
Vice President Operations

Mark Kearl
Vice President Finance and Chief Financial Officer

Russ Strilchuk
Vice President Sales and Marketing

Terence Bell
General Counsel and Corporate Secretary

CHINOOK DRILLING, a division of
Total Energy Services Inc.

Rod Rundell - General Manager

TOTAL OILFIELD RENTALS LIMITED PARTNERSHIP

Gerry Crawford - General Manager

BIDELL EQUIPMENT LIMITED PARTNERSHIP

Sean Ulmer - President

CORPORATE INFORMATION

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Calgary, Alberta

BANKER
HSBC
Calgary, Alberta

STOCK EXCHANGE LISTING

Toronto Stock Exchange

Symbol: TOT

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Fox Creek • Grande Prairie • High Level • Lac La Biche • Lloydminster • Manning • Medicine Hat • Peace River
Red Deer • Red Earth • Rocky Mountain House • Valleyview • Weyburn/Midale • Whitecourt



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