

Independent Auditor's Report

To the Shareholders of High Arctic Energy Services Inc.

We have audited the accompanying consolidated financial statements of High Arctic Energy Services Inc. and its subsidiaries, which comprise the consolidated balance sheets as at December 31, 2010 and December 31, 2009 and the consolidated statements of net earnings (loss), comprehensive income (loss) and deficit and cash flows for the year then ended, and the related notes including a summary of significant accounting policies.

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.

Auditor's 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 the auditor's 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, the auditor considers 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 financial position of High Arctic Energy Services Inc. and its subsidiaries as at December 31, 2010 and December 31, 2009 and the results of its operations and cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

PricewaterhouseCoopers LLP

Chartered Accountants
March 10, 2011

High Arctic Energy Services Inc.

Consolidated Balance Sheets

As at December 31, 2010 and 2009

(\$ Million)

	December 31, 2010	December 31, 2009
Assets		
Current assets		
Cash and cash equivalents	24.3	27.6
Accounts receivable (Note 12)	16.0	14.5
Inventory	2.5	2.8
Prepaid expenses	0.7	1.1
Assets related to Middle East discontinued operations (Note 15)	-	0.6
	<u>43.5</u>	<u>46.6</u>
Property and equipment (Note 3)	46.4	47.6
Assets held for sale including assets related to discontinued operations in the Middle East (Notes 3 and 15)	1.7	16.6
	<u>91.6</u>	<u>110.8</u>
Current liabilities		
Accounts payable and accrued liabilities	11.2	14.9
Income taxes payable	0.4	0.4
Due to related parties (Note 8)	-	7.0
Credit facility (Note 4)	36.5	65.4
Future income tax liabilities (Note 9)	0.7	0.7
Liabilities related to Middle East discontinued operations (Note 15)	-	0.3
Convertible debentures (Note 5)	-	27.9
	<u>48.8</u>	<u>116.6</u>
Shareholders' equity (deficiency) (Note 6)	<u>42.8</u>	<u>(5.8)</u>
	<u>91.6</u>	<u>110.8</u>
Commitments and contingencies (Note 10)		
See accompanying notes		

Approved on behalf of the Corporation by:

(signed) "Michael Binnion" Director

(signed) "Christopher Warren" Director

High Arctic Energy Services Inc.

Consolidated Statements of Net Earnings (loss), Comprehensive Income (loss) and Deficit

For the years ended December 31, 2010 and 2009

(\$ Million except per share amounts)

	2010	2009
Revenue (Note 13)	119.3	122.6
Expenses		
Oilfield services	77.3	84.7
General and administration	7.7	7.8
Share based compensation (Note 7)	1.9	0.4
Amortization	7.8	9.3
Foreign exchange loss	1.8	6.4
	<u>96.5</u>	<u>108.6</u>
Operating earnings	22.8	14.0
Interest	5.2	11.3
Financing costs	0.1	0.3
Gain on sale of property, equipment and investments	-	(0.9)
Gain on restructuring transactions (Note 6)	(2.6)	-
Gain on the sale of joint venture interest (Note 15b)	-	(2.4)
Impairment on assets held for sale and property and equipment (Note 3)	-	11.8
Net earnings (loss) before income taxes and discontinued operations	<u>20.1</u>	<u>(6.1)</u>
Income taxes (Note 9)	6.4	7.2
Earnings (loss) from continuing operations	<u>13.7</u>	<u>(13.3)</u>
Middle East discontinued operations, net of tax (Note 15a)	(0.9)	(0.8)
Optimal discontinued operations, net of tax (Note 15b)	-	(2.4)
Net earnings (loss) and comprehensive gain (loss)	<u>12.8</u>	<u>(16.5)</u>
Deficit – beginning of year	(141.7)	(125.2)
Deficit– end of year	<u>(128.9)</u>	<u>(141.7)</u>
Net earnings (loss) per share		
- basic and diluted from continuing operations	\$ 0.09	\$ (0.29)
- basic and diluted from discontinued operations	\$ (0.01)	\$ (0.07)
- basic and diluted from operations	\$ 0.08	\$ (0.36)

See accompanying notes

High Arctic Energy Services Inc.

Consolidated Statements of Cash Flows

For the years ended December 31, 2010 and 2009

(\$ Million)

Cash provided by (used in):	2010	2009
Operating activities		
Net earnings (loss) from continued operations	13.7	(13.3)
Add non-cash items:		
Amortization	7.8	9.3
Financing accretion and amortization	-	2.6
Share-based compensation (Note 7)	1.9	0.4
Impairment on assets held for sale (Note 3)	-	11.8
Future income tax (Note 9)	-	0.5
Gain on restructuring transactions	(5.0)	
Gain on sale of property and equipment	-	(0.9)
Gain on the sale of joint venture interest (Note 15b)	-	(2.4)
	<u>18.4</u>	<u>8.0</u>
Change in non-cash working capital balances (Note 14)	(0.8)	(4.6)
Cash flows from continuing operating activities	<u>17.6</u>	<u>3.4</u>
Investing activities		
Property and equipment and rigs and equipment under construction	(6.7)	(3.6)
Advances from Optimal Drilling	-	1.0
Proceeds on sale of property and equipment	8.1	1.3
Proceeds on sale of joint venture interest (Note 15b)	-	23.5
Change in non-cash working capital balances (Note 14)	-	(0.2)
	<u>1.4</u>	<u>22.0</u>
Financing activities		
Advances from related parties (Note 8)	0.2	0.7
Change in credit facility (Note 4)	(28.9)	(28.5)
Issuance of shares, net of costs (Note 6)	0.1	0.6
	<u>(28.6)</u>	<u>(27.2)</u>
Net change in cash from continuing operations	<u>(9.6)</u>	<u>(1.8)</u>
Cash flow from discontinued operations		
Operating activities	(0.5)	4.7
Investing activities		
Proceeds on sales of property and equipment	6.8	3.9
Property and equipment and rigs and equipment under construction	-	(1.4)
Net change in cash from discontinued operations	<u>6.3</u>	<u>7.2</u>
Net increase in cash and cash equivalents	(3.3)	5.4
Cash and cash equivalents – beginning of year	<u>27.6</u>	<u>22.2</u>
Cash and cash equivalents – end of year	<u>24.3</u>	<u>27.6</u>
Supplemental information (Note 14)		
Cash paid for:		
Interest	3.5	4.9
Income taxes	6.1	14.3

High Arctic Energy Services Inc.

Notes to the Consolidated Financial Statements

For the year ended December 31, 2010 and 2009

(\$ Million)

1 Basis of Presentation

High Arctic Energy Services Inc. (the "Corporation") is incorporated under the laws of Alberta, Canada, with a principal focus to provide contract drilling and workover services and other oilfield services to the oil and gas industry in Canada and Papua New Guinea. The Canadian operations are considered to have some seasonality with peak levels in the first and fourth quarters.

2 Accounting Policies

Measurement Uncertainty

The preparation of financial statements in conformity with Canadian GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the period. Such estimates include the amortization of property and equipment, recoverability of accounts receivable, valuation of unit-based compensation, accruals for contingencies, valuation of the convertible debenture components, future tax valuation allowance and impairment of property and equipment. Accordingly, actual results could differ from estimated amounts as future confirming events occur and the impact could be material.

Changes in Accounting Policy

New Accounting Standards Adopted

On January 1, 2010, the Corporation adopted the following Canadian Institute of Chartered Accountants (CICA) Handbook sections:

- "Business Combinations", Section 1582, which replaces the previous business combinations standard. The standard requires assets and liabilities acquired in a business combination, contingent consideration and certain acquired contingencies to be measured at their fair values as of the date of acquisition. In addition, acquisition-related and restructuring costs are to be recognized separately from the business combination and included in the statement of earnings. The adoption of this standard has had no material impact on the accounting treatment of business combinations entered into after January 1, 2010.
- "Consolidated Financial Statements", Section 1601, which, together with Section 1602 below, replace the former consolidated financial statements standard. Section 1601 establishes the requirements for the preparation of consolidated financial statements. The adoption of this standard has had no material impact on the Corporation's Consolidated Financial Statements.
- "Non-controlling Interests", Section 1602, which establishes the accounting for a non-controlling interest in a subsidiary in the consolidated financial statements subsequent to a business combination. The standard requires a non-controlling interest in a subsidiary to be classified as a separate component of equity. In addition, net earnings and components of other comprehensive income are attributed to both the parent and non-controlling interest. The adoption of this standard has had no material impact on the Corporation's Consolidated Financial Statements.

The above CICA Handbook sections are converged with IFRS. The Corporation will be required to report its results in accordance with IFRS beginning in 2011.

International Financial Reporting Standards

Effective January 1, 2011, the Corporation will be required to report its Consolidated Financial Statements in accordance with IFRS, including 2010 comparative information. The Corporation is in the final stages of its IFRS changeover plan and expects to report its first quarter 2011 results in accordance with IFRS. Based on current International standards, the Corporation expects the transition to IFRS will not have a major impact on the Corporation's operations, strategic decisions or cash flows.

High Arctic Energy Services Inc.

Notes to the Consolidated Financial Statements

For the year ended December 31, 2010 and 2009

(\$ Million)

Comparative Figures

Certain comparative figures have been reclassified to conform to the current financial statement presentation.

Principles of Consolidation

These financial statements represent the accounts of the Corporation and its principal wholly-owned foreign operating subsidiaries – High Arctic Energy Cyprus Ltd., High Arctic Energy Services PNG Limited, High Arctic Energy Services PTY Ltd, and High Arctic Energy Services LLC – and all other wholly-owned subsidiaries.

Cash and Cash Equivalents

Cash and cash equivalents are comprised of cash and short-term market investments that are highly liquid in nature and have an original maturity date of less than three months.

Inventory

Inventory consists primarily of operating supplies and spare parts not held for sale and is valued at the lower of cost and net realizable value, with cost determined using the weighted average cost method.

Financing Costs

Costs incurred to negotiate new debt or modify existing debt prior to its issuance are deferred and amortized over the term of the related debt provided the receipt of funding is probable. After the facility is operative, such costs are deducted from the related debt and amortized using the effective interest rate method. Any financing costs pertaining to negotiations that are subsequently abandoned are expensed at the time of abandonment.

Property and Equipment

Property and equipment are recorded at cost less accumulated amortization. Equipment is amortized using the declining balance method over their estimated useful lives at the following rates:

Automotive	30%
Computer hardware	30%
Computer software	100%
Equipment – rental, support and shop	10-30%
Equipment - drilling support	10%
Equipment - hydraulic workover rigs and UB rigs	10-30%
Equipment – stand alone, rig assist and nitrogen pumping	10-30%
Equipment - office	20%
Leasehold improvements	Lease term or five years

Management assesses the carrying amount of property and equipment for impairment when events indicate the carrying amount may not be recoverable. In such circumstances, an impairment loss is recognized in earnings for the amount by which the carrying amount exceeds fair value determined using an estimate of discounted future cash flows of operating equipment attributed to the property and equipment. If the asset has been classed as held for sale, the fair value is determined as the estimated sales value.

Work-in-Progress

Design and construction costs related to equipment under construction, including all costs to prepare the asset for its intended use and interest capitalized during the construction period, are recorded as Work-in Progress and are not subject to amortization until the asset is placed into service.

High Arctic Energy Services Inc.

Notes to the Consolidated Financial Statements

For the year ended December 31, 2010 and 2009

(\$ Million)

Investments

Investments in other companies over which the Corporation does not have significant influence are accounted for by the cost method. Investments are written down to their net realizable value should a decline in value occur that is other than temporary.

Income Taxes

The Corporation and its subsidiaries use the liability method of tax allocation in accounting for income taxes. Under this method, future tax assets and liabilities are determined for the income tax consequences attributable to differences between amounts recorded in the financial statements and their respective tax basis, using substantially enacted tax rates. The effect of any change in income tax rates on future tax assets and liabilities is recognized in earnings in the period that the change occurs. To the extent that the Corporation does not consider it to be more likely than not that a future tax asset will be recovered, it provides a valuation allowance against the excess.

Employee Benefit Plans

The Corporation provides a defined contribution pension plan for employees. Contributions by the Corporation are expensed when contributed. The Corporation has no other post-retirement benefit plans.

Foreign Currency Translation

The Corporation uses the Canadian dollar as its functional currency. Revenues and expenses denominated in foreign currencies are translated at the rate of exchange in effect on the date of the transaction.

The financial statements of the Corporation's foreign subsidiaries are translated using the temporal method. Monetary assets and liabilities of integrated foreign operations are translated using the rate of exchange in effect at the balance sheet date, whereas non-monetary assets and liabilities are translated at historical rates of exchange. Revenues and expenses are measured at average monthly exchange rates, except for amortization, which is determined using the historical exchange rate. Gains and losses resulting from translation are included in the statement of earnings.

Revenue Recognition

The Corporation's services include fixed or determinable prices based upon daily, hourly or job rates. The sales terms do not include provisions for significant post-service delivery obligations. Revenue is recognized when services are rendered or over equipment rental periods, and when collection is reasonably assured. Mobilization revenue is earned under certain contracts and is generally payable to the Corporation upon successful commencement of operations under the contract. For a contract that includes this element in addition to the normal fee for service element, revenue is allocated to each element of the contract based on the residual method and using the estimated fair value of the elements delivered. The value of the undelivered elements is deferred and recognized when earned. The Corporation defers prepaid mobilization revenues and recognizes them at the time the related services are performed using the percentage of completion method. Revenue for services under the contract are recognized as the service is provided based upon the fair value of the services.

Share-based Compensation Plans

The Corporation has a Share Option Plan which is described in Note 7. The fair value of share purchase options is calculated at the date of the grant using the Black-Scholes option pricing model. The value is recorded as compensation expense over the grant's vesting period, with an offsetting credit to contributed surplus. Upon exercise of the share purchase option, the associated amount is reclassified from contributed surplus to share capital. Consideration received from employees upon exercise of options is credited to shareholders' capital.

Per Share Amounts

Basic per share amounts are calculated using the weighted average number of shares outstanding during the year. Diluted per share amounts are calculated giving effect to the potential dilution that would occur if stock options, warrants and convertible debentures were exercised or converted into common shares.

High Arctic Energy Services Inc.

Notes to the Consolidated Financial Statements

For the year ended December 31, 2010 and 2009

(\$ Million)

Transaction Costs on Debt Issuance

The Corporation requires costs related to obtain debt financing be deducted from the related debt and amortized over the term of the debt as interest expense using the effective interest rate method.

Financial Instruments

Financial Instruments are accounted for based on one of five classifications: held for trading, held-to-maturity, other financial liabilities, loans and receivables or available-for-sale. The classification of a financial instrument depends on its characteristics and the purpose for which it was acquired.

A) Held for trading

Held for trading financial instruments are financial assets or financial liabilities that are purchased with the intention of selling or repurchasing in the near term. Any financial instrument can be designated as held for trading as long as its fair value can be reliably measured. A derivative is classified as held for trading unless designated as and considered an effective hedge. Held for trading instruments are recorded at fair value with any subsequent gains or losses from changes in the fair value included in earnings.

B) Held-to-maturity

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and a fixed maturity that the Corporation has the intent and ability to hold to maturity.

These financial assets are measured at amortized cost using the effective interest method. Any gains or losses arising from the sale of a held-to-maturity investment are included in earnings. All of the Corporation's cash equivalents are designate as held-to-maturity investments. The fair value of cash and cash equivalents approximate their carrying value due to their short-term nature.

C) Other financial liabilities

Items classified as other financial liabilities on the Corporation's financial statements are accounted for at amortized cost using the effective interest method. Any gains or losses in the realization of other financial liabilities are included in earnings. The fair value of accounts payable and accrued liabilities and the demand portion of any amounts due to related parties approximate their carrying values due to the short-term nature of these instruments. The fair value of the credit facility and the interest bearing amount due to related parties are recorded at values that estimate the fair value as the interest payable reflects market rates.

D) Loans and receivables

Items classified as loans and receivables in the Corporation's financial statements are accounted for at amortized cost using the effective interest method. Any gains or losses on the realization of loans and receivables are included in earnings. The fair value of accounts and other receivables and the demand portion of any amounts due from related parties approximate their carrying values due to the short-term nature of these instruments.

E) Available-for-sale

Available-for-sale assets are those financial assets that are not classified as held for trading, held-to-maturity or loans and receivables. Available-for-sale instruments are recorded at fair value. Any gains or losses arising from the change in fair value are recorded in Other Comprehensive Income and upon the sale of the instrument or other-than-temporary impairment, the cumulative gain or loss is include in earnings.

High Arctic Energy Services Inc.

Notes to the Consolidated Financial Statements

For the year ended December 31, 2010 and 2009

(\$ Million)

F) Derivative financial instruments

A derivative is a financial instrument whose value changes in response to a specified variable, requires little or no net investment and is settled at a future date. An embedded derivative is a derivative that is part of a non-derivative contract and not directly related to that contract. Embedded derivatives that are not closely related to the host contract must be accounted for as a separate financial instrument. A non-financial derivative is a contract that can be settled net in cash or another financial instrument. Fair values are based upon quoted market prices available from active markets or are otherwise determined using a variety of valuation techniques and models using quoted market prices.

The Corporation may enter into derivative contracts in order to manage risks. These contracts are marked to market at each reporting interval, with the change in estimated fair value recorded as a gain or loss in the period. The Corporation does not use derivative contracts for speculative or hedging purposes at this time. Currently, the Corporation has no qualifying hedging instruments, but in the future may designate any qualifying hedging instrument as a hedge for accounting purposes.

High Arctic Energy Services Inc.

Notes to the Consolidated Financial Statements

For the year ended December 31, 2010 and 2009

(\$ Million)

3 Property and Equipment

December 31, 2010

	Cost	Accumulated Amortization	Net
Automotive	3.4	1.7	1.7
Computer hardware	0.6	0.4	0.2
Computer software	0.9	0.8	0.1
Equipment – rental, support and shop	10.1	6.2	3.9
Equipment – drilling support	13.9	7.1	6.8
Equipment – hydraulic workover and UB rigs	28.2	18.2	10.0
Equipment – stand alone, rig assist and nitrogen pumping	56.1	35.1	21.0
Equipment – office	0.5	0.4	0.1
Leasehold improvements	0.5	0.1	0.4
Work-in-progress	2.2	-	2.2
	<u>116.4</u>	<u>70.0</u>	<u>46.4</u>

December 31, 2009

	Cost	Accumulated Amortization	Net
Automotive	3.0	1.3	1.7
Computer hardware	0.5	0.3	0.2
Computer software	0.9	0.7	0.2
Equipment – rental, support and shop	9.9	5.4	4.5
Equipment – drilling support	9.7	4.8	4.9
Equipment – hydraulic workover and UB rigs	28.3	17.9	10.4
Equipment – stand alone, rig assist and nitrogen pumping	55.7	31.3	24.4
Equipment – office	0.5	0.4	0.1
Leasehold improvements	0.4	-	0.4
Work-in-progress	0.8	-	0.8
	<u>109.7</u>	<u>62.1</u>	<u>47.6</u>

The Corporation provided for an impairment of \$11.8 million in 2009 related to:

- equipment classified as assets held for sale that was sold on January 13, 2010 resulting in additional write-downs on a heli-portable rig of \$0.1 million and on a RAPAD Rig of \$3.1 million;
- other equipment classified as assets held for sale resulting in a write-down of \$1.8 million; and
- equipment used in the operations resulting in a write-down of \$6.8 million primarily related to its three 250K UB rigs.

High Arctic Energy Services Inc.

Notes to the Consolidated Financial Statements

For the year ended December 31, 2010 and 2009

(\$ Million)

Management assessed the property and equipment balances for evidence of impairments using indicators such as declining market activity, changes in future expected cash flows from operations and, where appropriate, expected costs of disposition.

Evidence of impairment was assessed using an undiscounted cash flow test and where the net book value exceeded the undiscounted cash flow analysis a determination of the assets' fair market value was estimated.

The estimated fair market value was assessed by management using internal experts. The measurement of the impairment was assessed as the amount by which the carrying amount of an asset exceeded its fair market value.

In addition to the amounts reported in property and equipment at December 31, 2010, the Corporation had property and equipment classified and recorded as assets held for sale including assets related to discontinued operations of \$1.7 million (December 31, 2009 - \$16.6 million). The following amounts are included in the balance:

Assets held for sale including assets related to discontinued operations	December 31, 2010	December 31, 2009
Equipment held for sale in Canada	1.7	9.6
Equipment held for sale related to discontinued operations from the Middle East (Note 15a)	-	7.0
	<u>1.7</u>	<u>16.6</u>

4 Credit Facility

The Corporation had a revolving credit facility and a bridge facility credit agreement (collectively the "Original Senior Debt") that was restructured as part of the restructuring transactions completed on April 30, 2010 (see Note 6). On that date, the balances were combined into a single term loan facility with a maturity date of April 30, 2011. The Corporation also paid \$10.0 million to the senior lenders of which \$2.8 million was applied to repay outstanding fees from prior years and the 2% default interest described below, \$0.4 million was applied as an amendment fee related to the new term loan facility and the remaining \$6.8 million was applied against the loan principal. On closing, the principal amount of the term loan facility was \$43.9 million.

As at December 31, 2010, the Corporation owed \$36.5 million on the term loan facility (2009 – an aggregate of \$65.4 million on the Original Senior Debt). The interest rate applicable to the term loan facility commencing May 1, 2010 is prime plus 4.75% provided that prime has a floor amount of 4.75%. As a result, the minimum interest rate is 9.5%. Prior to May 1, 2010, the interest rate applicable to the revolving credit facility was prime plus 2% for amounts drawn up to 2.75x consolidated earnings before interest, depreciation, amortization and taxes and prime plus 4% for the excess drawn over the 2.75x amount and the interest rate applicable to the Bridge Loan was prime plus 6.25%. The Corporation was subject to an additional 2% per annum interest charge from July 1, 2009 until April 30, 2010 as a result of the event of default caused by its failure to repay the Original Senior Debt on the maturity date.

The term loan facility is due at the maturity date of April 30, 2011. Until then, there are no fixed amortization obligations but payments during the term will be required if the financial results of the Corporation exceed the agreed upon projections. Based on the financial results at December 31, 2010, the Corporation estimates it must make a payment in March, 2011 of approximately \$10.5 million which will be applied to reduce the principal amount of the term loan. The obligations under the term loan facility are secured by, among other things, the pledge of accounts receivable and the eligible equipment pursuant to debentures under which the Corporation and its subsidiaries grant security over all of their respective assets.

The consolidated leverage ratio ("CLR") is one of the key financial ratio covenants under the term loan facility and is a key measure used by the Corporation in assessing the progress made to reduce its leverage. The CLR is defined in the term loan facility agreement as, in general terms, consolidated total debt, as defined, divided by the 12-month trailing adjusted consolidated earnings before interest, depreciation, amortization and taxes. The CLR covenant is applied monthly and the maximum allowable ratio for the month ended April 30,

High Arctic Energy Services Inc.

Notes to the Consolidated Financial Statements

For the year ended December 31, 2010 and 2009

(\$ Million)

2010 was 2.25 to 1.00, for each month ended from May 31, 2010 until September 30, 2010 is 2.75 to 1.00 and thereafter is 2.25 to 1.00. As at December 31, 2010, the Corporation had a CLR of approximately 1.2 to 1.0.

The Corporation issued 12,630,740 common shares to the lenders as consideration for the new term loan facility on April 30, 2010. The Corporation has valued the shares at \$2.5 million and this amount was expensed as explained in Note 6. As part of the loan amendments in 2007 and 2008, the Corporation issued to its lenders 1,500,000 warrants to purchase common shares of the Corporation until June 20, 2010 at an exercise price of \$1.09 per common share. The warrants all expired without any being exercised.

5 Convertible Debentures

In November 2007, the Corporation issued \$27.9 million principal amount of unsecured convertible debentures (the "Debentures") with a maturity date of December 31, 2012. Costs related to the issuance of the Debentures were \$1.9 million, of which \$1.7 million was deducted against the related debt and amortized. The costs related to the issuance of the Debentures were fully amortized as at December 31, 2009.

As part of restructuring transactions completed on April 30, 2010 (see Note 6), the entire principal amount and all accrued and unpaid interest owing under the Debentures was converted into 123,681,133 common shares of the Corporation. The principal amount of \$27.9 million was converted into 111,592,000 common shares in full settlement of all outstanding principal owing plus 12,089,133 common shares were issued in full settlement of all accrued interest owing to the holders of the Debentures. The Corporation had accrued interest of \$3.7 million up to completion of the restructuring transactions on April 30, 2010.

Share capital of 123,681,133 common shares issued in settlement of the principal and interest was recorded at the estimated market value of \$24.7 million resulting in a gain on settlement of \$6.9 million recognized during the second quarter (See Note 6).

Prior to the restructuring transactions, the Debentures were considered a compound financial instrument and the liability and equity components were presented separately. The Debentures had been accounted for using the residual method, resulting in an equity element stemming from the call option in the amount of \$2.8 million, net of related issue costs of \$0.2 million, being credited to shareholders' equity. The liability was valued using an estimated borrowing rate of 16% and was fully accreted as at December 31, 2009.

High Arctic Energy Services Inc.

Notes to the Consolidated Financial Statements

For the year ended December 31, 2010 and 2009

(\$ Million)

6 Share Capital

(a) Details of Shareholders equity (deficiency)

Authorized

An unlimited number of common shares and an unlimited number of preferred shares may be issued.

Issued	December 31, 2010	December 31, 2009
Common shares (b)	165.4	126.9
Warrants	1.7	1.7
Equity element of convertible debentures (Note 5)	-	2.8
Contributed surplus (c)	4.6	4.5
Deficit	(128.9)	(141.7)
	<u>42.8</u>	<u>(5.8)</u>

(b) Changes in Issued Shares

	December 31, 2010		December 31, 2009	
	Shares	\$	Shares	\$
Opening Balance	45,442,325	126.9	42,442,325	126.3
Issuance of Shares	696,140	0.1	3,000,000	0.6
Issuance of Shares on restructuring transactions	169,280,257	36.6	-	-
Common Shares Outstanding	<u>215,418,722</u>	<u>163.6</u>	<u>45,442,325</u>	<u>126.9</u>
Restricted shares issued under the Share incentive Plan	35,500,000	1.8	-	-
	<u>250,918,722</u>	<u>165.4</u>	<u>45,442,315</u>	<u>126.9</u>

Restricted shares issued under the Share incentive Plan

On September 1, 2010, the Corporation issued 35,500,000 shares under the Share Incentive Plan (Note 7) to a trustee for the benefit of designated directors and executive management. The number of shares has been reflected under the total issued and outstanding common shares while the value of these shares will be included in the Common Share capital amount as they vest over the 3 year vesting period. These shares vest to each designated beneficiary over a 3 year period and a share capital amount of \$0.165 per share will be recorded as the related stock based compensation expense is recognized. The designated beneficiaries of the restricted common shares held in trust have full voting, liquidity, dividend and other related rights similar to the holders of the unrestricted issued shares. The shares are not freely tradable prior to vesting and any shares that do meet the vesting conditions will be returned by the trustee to the Corporation for cancellation.

Issuance of Shares

On January 23, 2009, the Corporation issued 3,000,000 common shares to certain directors and senior officers of the Corporation at an issue price of \$0.20 per share. The offering was completed as a non-brokered private placement, whereby certain officers and directors reinvested bonus amounts paid to them by the Corporation.

On December 23, 2010 the Corporation issued 625,000 common shares at an issue price of \$0.22 per share. The transaction was completed as a non-brokered private placement as part of an arrangement to settle an outstanding obligation.

For the year ending December 31, 2010, a total of 71,140 stock options were exercised for shares of the Corporation (see Note 7).

High Arctic Energy Services Inc.

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For the year ended December 31, 2010 and 2009

(\$ Million)

Restructuring transactions

On April 30, 2010 the Corporation completed a series of restructuring transactions to reduce debt levels and to meet the requirements for an extension of the credit facilities (see Note 4). Under the restructuring transactions, the Corporation:

- issued 32,968,384 common shares in settlement of all outstanding indebtedness and claims owing by the Corporation to related parties (see Note 8);
- converted the Corporation's outstanding Debentures into 111,592,000 common shares in full settlement of all outstanding principal of \$27,898,000 plus 12,089,133 common shares in full settlement of all accrued interest owed to the holders of the Debentures (see Note 5); and
- issued 12,630,740 common shares to its senior lenders as consideration for a one year term loan to refinance the existing senior credit facilities (see Note 4).

The Corporation issued a total of 169,280,257 common shares as part of the restructuring transactions. The shares were issued at a nominal value of \$0.25 per share. The amount recorded in share capital for the 169,280,257 common shares is the estimated market value of \$36.6 million determined as the trading price of \$0.20 per share at the closing date. The restructuring transactions resulted in a gain of \$2.6 million being recorded. Details on the restructuring transactions are summarized as follows:

	Number of Shares	\$ value of Shares	Gain (Loss)
Issuance of common shares on related party debt settlement (Note 8)	32,968,384	6.6	0.6
Issuance of common shares on debenture conversion (Note 5)	123,681,133	24.7	6.9
Issuance of common shares for financing fee related to restructuring (Note 4)	12,630,740	2.5	(2.5)
Transfer of the equity portion of debentures to share capital on debenture conversion (Note 5)	-	2.8	-
Non-cash portion of gain on restructuring transactions			5.0
Fee on restructuring of credit facility	-	-	(0.4)
Restructuring costs	-	-	(2.0)
	169,280,257	36.6	2.6

(c) Contributed Surplus

	December 31, 2010	December 31, 2009
Opening Balance	4.5	4.1
Share-based compensation (Note 7)	0.1	0.4
Closing Balance	4.6	4.5

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(d) Per Share Amounts

The following table summarizes the weighted average number of common shares used in calculating basic and diluted earnings per share. All potentially dilutive instruments such as options, the Executive and Director Share Incentive Plan, warrants and the convertible debentures are anti-dilutive.

	December 31, 2010	December 31, 2009
Number of common shares used in basic and diluted earnings per share	159,110,336	45,442,325

7 Share-based Compensation

Stock Option Plan

The Corporation has a Stock Option Plan under which options to purchase common shares may be granted to directors, management and key employees. A total of 25,091,872 options (being 10% of all outstanding shares) are available for grants.

At December 31, 2010, a total of 5,727,400 options are outstanding and expire at various dates up to 2015, at amounts that range from \$0.13 to \$12.61 per share. These options are exercisable over a term of 5 years and are subject to a three-year vesting period with 40% exercisable by the holder after the first anniversary date, 70% after the second anniversary date and 100% after the third anniversary date. The options have an average remaining contractual life of 4.03 years and 1,176,450 options are currently vested and eligible to be exercised.

	Number of Options	Weighted Average Exercise Price \$/Share
Total Outstanding January 1, 2009	1,186,900	3.88
Granted	3,260,100	0.15
Exercised	-	-
Cancelled	(670,000)	1.88
Forfeited	(566,450)	2.26
Total Outstanding December 31, 2009	3,210,550	0.79
Granted	3,087,500	0.20
Exercised	(71,140)	0.15
Expired	(59,500)	10.53
Forfeited	(440,010)	1.15
Total Outstanding December 31, 2010	5,727,400	0.35

High Arctic Energy Services Inc.

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Exercise Price Range	Options Outstanding			Exercisable Options	
	Number of Options	Remaining Contractual Life (Years)	Weighted Average Exercise Price (\$)	Number of Options	Weighted Average Exercise Price (\$)
\$0.13 to \$1.99	5,565,750	4.11	0.19	1,015,300	0.21
\$2.00 to \$3.99	75,150	1.25	2.77	75,150	2.77
\$4.00 to \$6.99	30,500	0.96	6.03	30,500	6.03
\$7.00 to \$9.99	42,000	0.75	9.67	42,000	9.67
\$10.00 to \$12.61	14,000	0.53	11.83	14,000	11.83
Total Outstanding December 31, 2010	5,727,400	4.03	0.35	1,176,450	1.00

Share-based compensation expense was recognized by the Corporation for the year ended December 31, 2010 in the amount of \$0.1 (2009 - \$0.4 million) based on amortizing any expense over the vesting period using the Black-Scholes model. The options valued prior to December 31, 2007 used an average risk-free interest rate of 4.2%; average expected life of 5 years; expected volatility of 40% to December 31, 2007 and 75% thereafter and a weighted average estimate of distribution yield of nil. The 2008 options were valued using an average risk-free interest rate of 3.4%; average expected life of 5 years; expected volatility of 67.6% and an expected annual dividend yield of nil. The options in 2009 were valued with a weighted average expected volatility of 79.0%, a risk free interest rate of 1.61%, expected annual dividend yield of 0.0% and an expected life of 5 years. The options in 2010 were valued with a weighted average expected volatility of 96.6%, a risk free interest rate of 2.42%, expected annual dividend yield of 0.0% and an expected life of 5 years.

Share Incentive Plan

At the Annual General Meeting on June 29, 2010, the shareholders approved an Executive and Director Share Incentive Plan. The maximum number of common shares reserved for issuance by the Corporation under the plan is 37,892,220 common shares. On August 17, 2010, 35,500,000 shares were granted to executives and directors of the Corporation. The incentive shares have a three-year vesting period with 40% vesting on April 1, 2011, 30% on September 1, 2012 and 30% on September 1, 2013. Stock-based compensation will be recorded over the three year vesting period and \$1.8 million has been recorded for the year ended December 31, 2010.

8 Related Party Transactions

In the normal course of business, during the year ended December 31, 2010, the Corporation incurred general and administration expenses related to premises rent of \$0.4 million (2009 - \$1.0 million) and equipment and vehicle leases payments of approximately \$0.1 million respectively (2009 - \$0.3 million) charged by companies controlled by the person who, prior to the April 30, 2010 restructuring transactions, controlled almost 40% of the outstanding shares and who was the President and Chief Executive Officer of the Corporation until December 16, 2008 (the "Shareholder"). These transactions are measured at exchange values based on rates charged by arms length persons, which, in the opinion of management, approximate fair value.

As part of the restructuring transactions completed on April 30, 2010 (see Note 6), the Corporation issued 32,968,384 common shares to the Shareholder and companies controlled by him in settlement of the outstanding obligations owing by the Corporation on that date with a recorded amount of approximately \$7.2 million (2009 - \$7.0 million). Mutual releases were signed between the parties settling all outstanding litigation and other claims to April 30, 2010. The Corporation recorded the value of the 32,968,384 common shares as \$6.6 million resulting in a \$0.6 million gain on the settlement of the outstanding obligations that is included in the gain on restructuring transactions. Interest expense for the year ended December 31, 2010 includes \$0.2 million (2009 - \$0.5 million) in respect of the amounts that were settled with the Shareholder.

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(\$ Million)

9 Income Taxes

(a) Income Tax Expense

The tax provision for income tax in the consolidated statement of loss and deficit varies from the amount that would be computed by applying the expected income tax rate of 28% (2009 – 29%) to the loss before taxes. The principal reasons for differences between “expected” income tax and the amount actually recorded are as follows:

	December 31, 2010	December 31, 2009
Gain (loss) from continuing operations before income taxes	20.1	(6.1)
Loss from discontinued operations before income taxes	(0.9)	(2.9)
	<u>19.2</u>	<u>(9.0)</u>
Computed income tax recovery at the statutory rate	5.4	(2.6)
Increase (decrease) resulting from:		
Non-deductible expenses	0.5	0.7
Dividend taxes paid	0.9	-
Non deductible losses – International tax exempt countries	0.2	0.1
Revenue based taxes in foreign jurisdictions	-	0.3
Tax rate differences	0.8	1.0
Unrecognized tax losses associated with Optimal	-	0.9
Canadian losses and temporary differences not recognized for tax purposes	(1.4)	7.1
Income tax expense	<u>6.4</u>	<u>7.5</u>
Represented by:		
Current income tax on continuing operations	6.4	6.7
Future income tax on continuing operations	-	0.5
Current Income tax on discontinued operations	-	0.3
Future income tax on discontinued operations	-	-

(b) Future Income Tax Asset

Differences between the accounting and tax basis of assets and liabilities at the tax rates expected to apply upon the reversal of the differences are shown below. At December 31, 2010 the Corporation's future tax liability is in respect of its subsidiary operations in Papua New Guinea. The Corporation has recorded a valuation allowance against all Canadian temporary differences and tax benefits related to the sale of Optimal.

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	December 31, 2010	December 31, 2009
Property and equipment and assets held for sale – Canada	6.3	13.3
Temporary differences – Papua New Guinea	(0.7)	(0.7)
Financing costs	2.1	2.1
Non-capital losses carried forward	20.4	14.7
Net capital losses carried forward	0.9	1.1
Future Tax valuation allowance	(29.7)	(31.1)
Other	-	(0.1)
Future tax liability	<u>(0.7)</u>	<u>(0.7)</u>

At December 31, 2010, the Canadian non-capital losses carried forward for income tax purposes was \$81.4 million (2009 – \$58.6 million) which expire in 2027, 2028, 2029 and 2030. Also at December 31, 2010, the Canadian net capital losses carried forward for income tax purposes was \$3.7 million (2009 – \$4.6) which can be used indefinitely but only against taxable capital gains. The Corporation has the ability to file amended tax returns to adjust certain discretionary deductions to mitigate the risk of expiring loss carry forwards.

10 Commitments and Contingencies

Accounts Receivable

The Corporation has commenced litigation against a customer with respect to collection of a receivable for services rendered outside Canada. The Corporation believes it has made an adequate provision for the possibility of non-collectable amounts and the receivable has been insured with the Export Development Canada (EDC). The customer has made a number of allegations and initiated a counter claim of \$5 million concerning performance issues and the cashing of the letter of credit of \$1.0 million. The Corporation has not recorded an accrual in relation to the counter claim as management believes that the claim is without merit and no details have yet been supplied by the claimant.

Other

The Corporation has posted a performance bond that has been guaranteed by Export Development Canada (“EDC”) of approximately US\$3.5 million, in respect of a contract in the Middle East region, and would be liable to EDC if the bond was called as a result of a default by the Corporation in the performance of its obligations under the contract. Under the terms of the contract, the Corporation could be obligated to provide up to five rigs that may not be available if requested. As at December 31, 2010, the Corporation was not providing any services under that contract. The term of the contract ends in August, 2012.

Lease Obligations

The Corporation has entered into various long-term premises leases in Canada. The minimum lease payments for the next five years as at December 31, 2010 are:

	\$
To December 31, 2011	0.5
To December 31, 2012	0.3
To December 31, 2013	0.3
To December 31, 2014	0.3
To December 31, 2015	0.1
	<u>1.5</u>

High Arctic Energy Services Inc.

Notes to the Consolidated Financial Statements

For the year ended December 31, 2010 and 2009

(\$ Million)

11 Capital Disclosures

The Corporation's capital structure is comprised of Shareholders' equity (deficiency), described in Note 6, and the credit facility described in Note 4.

	December 31, 2010	December 31, 2009
Shareholders' equity (deficiency)	42.8	(5.8)
Convertible Debentures	-	27.9
Credit facility	36.5	65.4
Cash and cash equivalents	(24.3)	(27.6)
Total Capitalization	55.0	59.9

The Corporation's goal is to have a capital structure that will provide the capital to meet the needs of its business and instill confidence with investors, creditors and capital markets. The Corporation has been focused on reducing its debt levels and increasing the shareholders' equity to reduce its leverage ratios and provide adequate financial flexibility to meet its financial obligations, both current and long term. Effective on April 30, 2010, the Corporation closed a restructuring transaction that included converting certain debt to equity so as to reduce the overall debt and increase equity (See Note 5 and Note 6). At the closing of the restructuring transaction, the Corporation made a \$6.8 million payment against its credit facilities and converted its senior credit facility into a term loan that matures on April 30, 2011 (See Note 4). On April 30, 2010 the term loan principal amount was \$43.9 million. The Corporation made principal payments on the term loan throughout 2010 and at December 31, 2010 the principal amount owing is \$36.5 million (2009 – \$65.4 million)

Future equity financings are a possibility to further reduce debt and raise capital for new business opportunities. Financing decisions for the foreseeable future will be governed largely by the requirement to manage the credit facility. Longer term, financing decisions will be based on the timing and extent of expected operating and capital cash outlays.

The Corporation monitors its debt levels and ability to service the debt using non-GAAP financial metrics with the primary one being the Consolidated Leverage Ratio or CLR. The CLR is defined in the term loan facility agreement as, in general terms, consolidated total debt, excluding the Convertible Debentures, as defined, divided by the 12-month trailing adjusted consolidated earnings before interest, depreciation, amortization and taxes (EBITDA). The Corporation's objective is to maintain the CLR at a level of 1.5 to 1.0, or better. At December 31, 2010 the CLR was 1.2 to 1.0 (2009 – 2.2 to 1.0).

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	Year Ended December 31, 2010	Year Ended December 31, 2009
Consolidated Total Debt	36.5	65.4
Net earnings (loss) and comprehensive gain (loss)	12.8	(16.5)
Add (deduct):		
Interest and financing	5.3	11.6
Income tax	6.4	7.2
Amortization	7.8	9.3
Gain on sale of property and equipment	-	(0.9)
Gain on sale of joint venture interest	-	(2.4)
Gain on restructuring transactions	(2.6)	-
Asset impairment	-	11.8
Foreign exchange loss	-	6.4
Stock based compensation	1.9	0.4
Adjustment for discontinued operations	0.1	0.1
Optimal Pressure Drilling Services	-	2.4
Adjusted EBITDA (Twelve Month)	31.7	29.4
Consolidated Leverage Ratio	1.2	2.2

12 Financial Instruments and Risk Management

Fair Value of Financial Assets and Liabilities

The Corporation's cash and cash equivalents are designated as held-for-trading and are measured at carrying value, which approximates fair value due to the short term nature of these instruments. Accounts receivable are designated as loans and receivables and recorded at amortized cost, which approximates fair value due to the short term nature of the instrument. Accounts payable and accrued liabilities and the credit facility are designated as other liabilities and are recorded at cost.

Financial Risks

The Corporation is exposed to financial risks arising from its financial assets and liabilities. The financial risks include market risk relating to interest rates, foreign currency risk, commodity price risk, credit risk and liquidity risk.

Market Risk

Market risk is the risk that the fair value or future cash flows of financial assets or liabilities will fluctuate due to movements in market rates of interest, foreign currency exchange rates and commodity prices.

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Interest Rate Risk

Interest rate risk is the risk that the value of a financial instrument will fluctuate as a result of changes in market interest rates. The Corporation is exposed to interest rate risk as the term loan is a floating rate credit facility and fluctuates in response to changes in the prime interest rates. For the year ended December 31, 2010, an increase or decrease in interest expense for each one percent change in interest rates on the term loan facility would have amounted to \$0.4 million.

Foreign Currency Risk

Foreign currency risk is the risk that a variation in the exchange rate between Canadian and foreign currencies will affect the Corporation's results. The majority of the Corporation's international revenue and expenses are transacted in U.S. dollars and the Corporation does not actively engage in foreign currency hedging.

For the year ended December 31, 2010, a 1% increase in the value of the Canadian dollar relative to the U.S. dollar would have resulted in a \$0.1 million decrease in earnings as a result of changes in foreign exchange.

Commodity Price Risk

Commodity price risk is the risk that fluctuations in oil or natural gas prices could materially adversely affect the Corporation's financial condition. The commodity prices affect the levels of drilling activity, which affects certain segments of the Corporation's business, particularly with respect to natural gas. The Corporation mitigates this exposure with its diversification into international operations not dependent on the Canadian oil and gas industry.

Credit Risk

Credit risk is the risk of a financial loss occurring as a result of a default by a counter party on its obligation to the Corporation. The Corporation's financial instruments that are exposed to credit risk consist primarily of accounts receivable and cash balances held in banks. The Corporation mitigates credit risk by regularly monitoring its accounts receivable position and depositing cash in properly capitalized banks. The Corporation also institutes detailed credit reviews prior to commencement of contractual arrangements and where practical uses export credit insurance provided by Export Development Canada.

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(\$ Million)

Customers

The Corporation's account receivables are predominantly with customers who explore for and develop petroleum reserves and are subject to normal industry credit risks. The Corporation assesses the credit worthiness of its customers on an ongoing basis and monitors the amount and age of balances outstanding. The Corporation views the credit risks on these amounts as normal for the industry. The carrying amount of accounts receivable represents the maximum credit exposure on this balance. The Corporation has a wide range of customers comprised of small independent, intermediate and large multinational oil and gas producers. Notwithstanding its large customer base, the Corporation has two significant customers. Services are provided to the first significant customer in Papua New Guinea. That customer represents approximately 55% of the Corporation's revenue for the year ended December 31, 2010 and 48% of its accounts receivable at that date. The second significant customer is a major Canadian exploration and production company which represents approximately 11% of the Corporation's revenue for the year ended December 31, 2010 and 10% of the Corporation's accounts receivable at that date. The services provided to this customer are distributed within this customer's diverse locations of operations within Canada, which management believes limits the risk of concentrating a significant portion of its revenue on this customer. Management has assessed the two customers as creditworthy and the Corporation has had no history of collection issues with either customer.

The aging of accounts receivables is as follows:

	December 31, 2010
0 to 30 days	8.2
31 to 60 days	5.5
61 to 90 days	1.3
Greater than 90 days	1.7
Allowances for doubtful debts	(0.7)
Total	16.0

The allowance for doubtful debts provision is based on an individual account by account analysis and the customer's prior credit history.

Liquidity Risk

Liquidity risk is the risk that the Corporation will not be able to meet its financial obligations as they fall due. The Corporation's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due. The Corporation's processes for managing liquidity risk include preparing and monitoring capital and operating budgets, coordinating and authorizing project expenditures, and authorization of contractual agreements. The Corporation seeks to manage its financing based on the results of these processes. The budgets are updated when required as conditions change (see Note 11).

The following are the contractual maturities of financial liabilities in the future fair value amounts:

	1 Year	2-3 Years	4-5 Years	Beyond 5 Years	Total
Accounts Payable	11.2	-	-	-	11.2
Credit Facility	36.5	-	-	-	36.5
Total	47.9	-	-	-	47.9

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13 Segmented Information

The Corporation operates one business of providing oilfield services to customers. This business has the following geographic characteristics:

Revenue	2010	2009
Canada	39.1	27.2
International		
Papua New Guinea	78.3	94.8
Other	1.9	0.6
Total International	80.2	95.4
	<u>119.3</u>	<u>122.6</u>
Property and equipment and Assets held for sale from continuing operations	2010	2009
Canada	31.7	43.1
Papua New Guinea	15.0	14.1
Other	1.4	-
	<u>48.1</u>	<u>57.2</u>

14 Supplementary Information

The net change in the following non-cash working capital items decreases cash flows was as follows:

	2010	2009
Operations		
Accounts receivable	(1.5)	8.5
Inventory and prepaid expenses	0.7	(0.9)
Accounts payable and accrued liabilities, income taxes payable, amortization of accrued fees and prepaid mobilization revenue	3.7	(12.2)
Gain on restructuring transaction	(3.7)	-
	<u>(0.8)</u>	<u>(4.6)</u>
Investing		
Accounts payable and accrued liabilities	-	(0.2)
	<u>(0.8)</u>	<u>(4.8)</u>

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Non-cash transactions include the following amounts:

	2010	2009
Issuance of common shares on debenture conversion	27.5	-
Issuance of common shares on related party debt settlement	6.6	-
Issuance of common shares for financing fee related to restructuring	2.5	-
	36.6	-

15 Discontinued Operations

(a) Middle East Region Discontinued Operations

A decision was made during 2008 to discontinue operations in the Middle East region, including Tunisia and India, due to ongoing losses. The Corporation has divested of assets through sales and has used the proceeds on sales to reduce its debt. At December 31, 2008 the remaining assets were classified as held for sale.

The Middle East region operations are in the same general industry as the other regions of the Corporation and therefore this region was not a separate segment. The cash flows of this component were tracked separately by management and were managed as a separate geographical oilfield service component within the overall corporate structure. Accordingly, it has been accounted for as a discontinued operation.

Comparative figures have been adjusted to remove activities in the Middle East region and to report those amounts as a discontinued operation. The following amounts have been included in the December 31, 2010 and December 31, 2009 Consolidated Balance Sheets.

	2010	2009
Current assets related to discontinued operations		
Accounts Receivable	-	0.6
Total current assets related to discontinued operations	-	0.6
Assets held for sale related to discontinued operations	-	7.0
Discontinued assets held for sale (Note 3)	-	7.0
	-	7.0
	2010	2009
Current liabilities related to discontinued operations		
Accounts payable and accrued liabilities	-	0.3
Total current liabilities related to discontinued operations	-	0.3

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The following amounts have been included in the results for the three and twelve months ended December 31, 2010 and 2009 Consolidated Statements of Net Earnings (Loss), Comprehensive Income (Loss) and Deficit:

	2010	2009
Revenue	-	1.5
Expenses		
Oilfield services	0.1	1.3
General and administration	0.7	0.9
Foreign exchange loss	-	0.2
Impairment on Assets Held for Sale	-	0.3
	<u>0.8</u>	<u>2.7</u>
Operating loss	(0.8)	(1.2)
Interest and financing fees	0.1	-
Gain on sale of property and equipment	-	(0.5)
Loss before income taxes	(0.9)	(0.7)
Income taxes	-	0.1
Discontinued Operations, net of tax	<u>(0.9)</u>	<u>(0.8)</u>

(b) Optimal Pressure Drilling Services Discontinued Operations

On December 31, 2007 the Corporation formed a joint venture ("Optimal Pressure Drilling Services") with a large international group for the purpose of providing underbalanced drilling services and managed pressure drilling. Optimal Pressure Drilling Services was owned 51% by the Corporation.

On September 25, 2009, the Corporation completed the sale of its entire interest in Optimal Pressure Drilling Services to its joint venture partner for aggregate gross proceeds of \$23.5 million. The Corporation reported a gain on sale, net of taxes, of \$2.4 million.

Summarized financial information (in CDN\$) for the Corporation's 51% proportionate interest in Optimal Pressure Drilling Services is as presented below. Balance Sheet amounts are not shown due to the sale on September 25, 2009 while Income Statement information represents the 51% proportionate results for the three and twelve months ended December 31, 2010 and December 31, 2009.

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	2010	2009
Revenue	-	8.4
Expenses		
Oilfield services	-	7.3
General and administration	-	0.4
Amortization	-	2.8
Foreign exchange loss	-	-
Interest	-	0.1
	<u>-</u>	<u>10.6</u>
Net loss before income taxes	-	(2.2)
Income taxes	-	0.2
Net loss	<u>-</u>	<u>(2.4)</u>

Certain adjustments are required to be made in determining the amounts reported as discontinued operations for the purposes of reporting in the Consolidated Financial Statements of High Arctic Energy Services Inc. The following schedule provides reconciliation between the 51% proportionate results reported above for the twelve months ended December 31, 2010 and December 31, 2009 and the loss from discontinued operations reported on the Income Statement.

	2010	2009
Net loss	-	(2.4)
Adjustments		
Foreign Exchange Adjustment on consolidation	-	-
Interest eliminated between consolidated entities	-	0.4
Amortization expense related to amortized gain	-	-
Discontinued Operations, net of tax	<u>-</u>	<u>(2.0)</u>