

## **MANAGEMENT'S DISCUSSION AND ANALYSIS FOR THE YEAR ENDED DECEMBER 31, 2009**

The following Management's Discussion and Analysis ("MD&A") of Essential Energy Services Trust ("Essential" or the "Trust") for the year ended December 31, 2009 should be read in conjunction with the Trust's audited consolidated financial statements as at and for the years ended December 31, 2009 and 2008 and the notes contained therein. This MD&A was prepared effective March 10, 2010.

### **FORWARD-LOOKING STATEMENTS**

*This MD&A contains forward-looking statements and forward-looking information within the meaning of applicable securities laws. The use of any of the words "expect", "anticipate", "continue", "estimate", "objective", "ongoing", "may", "will", "project", "should", "believe", "plans", "intends" and similar expressions are intended to identify forward-looking information or statements. In particular, this MD&A contains forward-looking statements including expectations as to the benefits and anticipated timing of the conversion to a corporation (the "Conversion"), plans of the Trust on completion of the Conversion and the effect thereof, expectations regarding the implementation of legislation, expectations regarding capital spending and cost saving measures, the sources of capital and uses of such capital, the services offered by the Trust and the relocation of these services to different geographic areas, expectations of future cash flow and earnings, expectations regarding the Trust's ability to access credit from its lenders, expectations with respect to the demand for and price of oil and natural gas including natural gas storage levels, expectations regarding the level and type of drilling and production activity in the Western Canadian Sedimentary Basin, expectations regarding the timing of the Alberta government's competitiveness review and the effects therefrom and expectations regarding the business, operations and revenues of the Trust in addition to general economic conditions. Although the Trust believes that the expectations and assumptions on which such forward-looking statements and information are based are reasonable, undue reliance should not be placed on the forward-looking statements and information because the Trust can give no assurance that they will prove to be correct. Since forward-looking statements and information address future events and conditions, by their very nature they involve inherent risks and uncertainties. Actual results could differ materially from those currently anticipated due to a number of factors and risks. These include, but are not limited to, the risks associated with the oilfield services sector (e.g. demand, pricing and terms for oilfield services; current and expected oil and gas prices; exploration and development costs and delays; reserves discovery and decline rates; pipeline and transportation capacity; weather, health, safety and environmental risks), integration of acquisitions, competition, and uncertainties resulting from potential delays or changes in plans with respect to acquisitions, development projects or capital expenditures and changes in legislation, including but not limited to tax laws, royalties and environmental regulations, risks associated with the potential inability to obtain required consents for the Conversion, including unit holder approval and court approval, failure to realize the benefits of the Conversion, stock market volatility and the inability to access sufficient capital from external and internal sources and the inability to pay dividends. Accordingly, readers should not place undue reliance on the forward-looking statements. Readers are cautioned that the foregoing list of factors is not exhaustive. Additional information on these and other factors that could affect the Trust's financial results are included in reports on file with applicable securities regulatory authorities and may be accessed through the SEDAR website ([www.sedar.com](http://www.sedar.com)). The forward-looking statements and information contained in this MD&A are made as of the date hereof and the Trust undertakes no obligation to update publicly or revise any forward-looking statements or information, whether as a result of new information, future events or otherwise, unless so required by applicable securities laws.*

## OVERVIEW OF ESSENTIAL

Based in Calgary, Essential is an open-end unincorporated, limited purpose investment trust. Essential provides oilfield services to oil and gas producers in western Canada related to the ongoing servicing of producing wells and new drilling activity.

The Trust's services are offered through two operating segments: Well Servicing and Wireline & Rentals. The Well Servicing segment provides production and completion services through its fleet of service rigs, rod rigs and coil tubing rigs. The Wireline & Rentals segment provides wireline and downhole tool sales, services and equipment rentals.

A third non-operating segment, Corporate, includes general and administrative costs and interest.

## BASIS OF PRESENTATION

The following MD&A, and the consolidated financial statements as at and for the year ended December 31, 2009 have been prepared in accordance with Canadian Generally Accepted Accounting Principles ("GAAP") except where otherwise indicated.

## SELECTED FINANCIAL INFORMATION

| (\$ Thousands, except per unit amounts)                | Three months ended<br>December 31, |           | Year ended<br>December 31, |           |
|--|------------------------------------|-----------|----------------------------|-----------|
|  | 2009                               | 2008      | 2009                       | 2008      |
| Revenue  | <b>30,108</b>                      | 43,842    | <b>111,722</b>             | 127,924   |
| Gross margin <sup>(1)</sup>                            | <b>6,764</b>                       | 12,086    | <b>19,479</b>              | 29,792    |
| Gross margin as a percentage of revenue <sup>(1)</sup> | <b>22%</b>                         | 28%       | <b>17%</b>                 | 23%       |
| EBITDAS <sup>(1)</sup> from continuing operations      | <b>4,586</b>                       | 8,219     | <b>10,021</b>              | 18,801    |
| EBITDAS as a percentage of revenue <sup>(1)</sup>      | <b>15%</b>                         | 19%       | <b>9%</b>                  | 15%       |
| Loss from continuing operations                        | <b>(1,409)</b>                     | (14,685)  | <b>(9,480)</b>             | (23,443)  |
| Per unit – basic and diluted                           | \$ <b>(0.02)</b>                   | \$ (0.25) | \$ <b>(0.16)</b>           | \$ (0.44) |
| Earnings (loss) from discontinued operations           | <b>n/a</b>                         | (1,265)   | <b>n/a</b>                 | 4,182     |
| Per unit – basic and diluted                           | <b>n/a</b>                         | \$ (0.02) | <b>n/a</b>                 | \$ 0.08   |
| Net loss   | <b>(1,409)</b>                     | (15,950)  | <b>(9,480)</b>             | (19,261)  |
| Per unit – basic and diluted                           | \$ <b>(0.02)</b>                   | \$ (0.27) | \$ <b>(0.16)</b>           | \$ (0.36) |
| Funds flow from operations <sup>(1)</sup>              | <b>4,374</b>                       | 6,113     | <b>8,791</b>               | 15,987    |
| Per unit – basic and diluted                           | \$ <b>0.07</b>                     | \$ 0.09   | \$ <b>0.15</b>             | \$ 0.30   |
| Distributions to Unitholders                           | -                                  | 2,703     | <b>3,191</b>               | 17,655    |
| Per unit   | \$ -                               | \$ 0.04   | \$ <b>0.05</b>             | \$ 0.33   |
| Total assets   | <b>169,380</b>                     | 192,035   | <b>169,380</b>             | 192,035   |
| Total long term debt                                   | <b>16,600</b>                      | 17,525    | <b>16,600</b>              | 17,525    |
| Unitholders' equity                                    | <b>143,367</b>                     | 154,824   | <b>143,367</b>             | 154,824   |

The acquisition of Builders Energy Services Trust ("Builders") on April 4, 2008 and the subsequent disposition of the Transport division on July 2, 2008 resulted in the following:

- The financial results of Builders have been included in the consolidated financial statements and MD&A of the Trust since April 4, 2008.
- The financial results of the Transport division have been reclassified under the caption of "Earnings (loss) from discontinued operations".

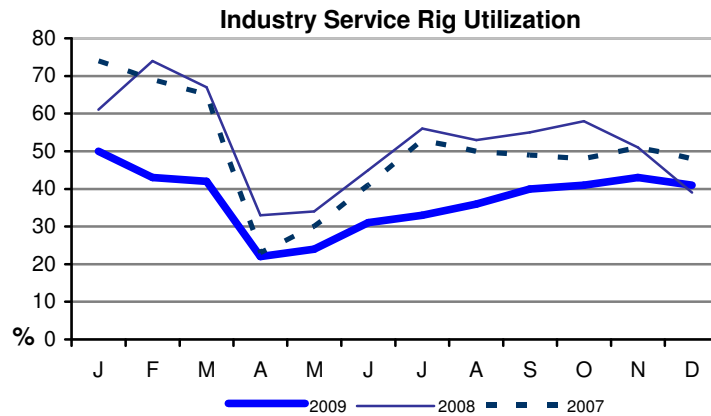
<sup>1</sup> Refer to "Non-GAAP Measures" section for further information.

**Additional Information**

Additional information regarding Essential, including the 2009 interim reports, 2008 Annual Report and the Annual Information Form for the year ended December 31, 2009, can be found on SEDAR at [www.sedar.com](http://www.sedar.com).

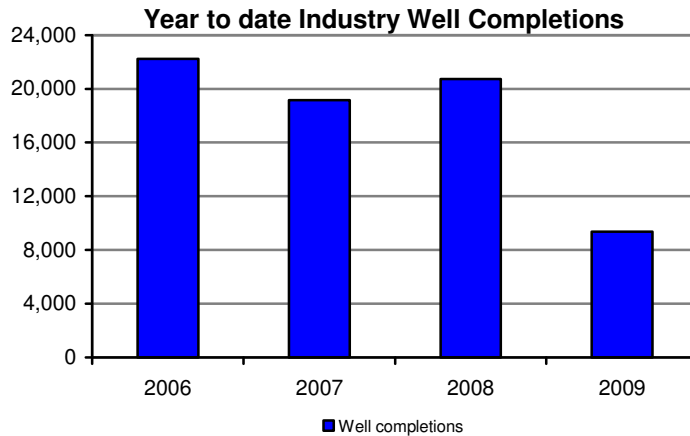
**OVERVIEW OF SECTOR ACTIVITY**

2009 was a test of resilience for the Canadian energy services sector as the downturn was far more pronounced than previous downturns due to decreased demand for oilfield services combined with the significant build up of equipment in the Western Canada Sedimentary Basin (“WCSB”) over the last few years. Service rig utilization within the WCSB peaked in early February and the following months saw utilization fall to near 20 year lows as depressed commodity prices, higher than expected natural gas storage levels, uncertainty with respect to the Alberta royalty regime and the reduced availability of credit caused exploration and production companies to reduce or defer exploration programs, production work and in some cases shut in natural gas production. Sector activity levels towards the end of the year began to improve as natural gas prices improved, oil prices stabilized and the renewed availability of credit resulted in exploration and production companies reinstating some of their drilling and completion programs.



Source: Canadian Association of Oilwell Drilling Contractors

Service rig utilization experienced a sharper decline in comparison to drilling rig utilization as some exploration and production companies undertook limited drilling activities to assess production and preserve lease rights but deferred completion activities and elected to leave wells shut in until natural gas prices improved. This resulted in a significant decline in well completions in 2009 compared to recent years. While this may lead to a backlog of service rig work in the future, in the short term it has negatively impacted service rig utilization.



Source: Canadian Association of Oilwell Drilling Contractors

Oilfield service companies experienced an erosion of prices throughout most of 2009 as a result of declining activity, extensive competition and surplus equipment. In the latter part of 2009 prices stabilized due to improving activity levels.

## OVERVIEW OF 2009 RESULTS

Throughout 2009, the Trust focused on cost cutting measures to mitigate the impact of reduced activity levels and competitive pricing pressures. However, even with aggressive cost cutting, the Trust has been adversely impacted by the overall decline in activity in the WCSB.

Notwithstanding these difficult operating conditions, the Trust experienced service growth success through the addition of a deep coil tubing rig and multi-stage fracturing services. These services expanded the Trust's capability within the Bakken, Montney and other resource plays.

As a result of improved activity levels, Essential's fourth quarter results exceeded management's expectations. Exploration and production companies began their winter drilling programs in November and the programs extended through to the end of December, benefiting all of Essential's service lines. This improved activity created labour challenges that the Trust was able to overcome through the steps taken earlier in the year that enabled the Trust to retain quality personnel. In spite of the improvements in utilization during the quarter, competitive market conditions continued to adversely impact pricing and margins.

## Financial Highlights

- Revenue from continuing operations for the year ended December 31, 2009 was \$111.7 million, compared to \$127.9 million for the year ended December 31, 2008.
- Gross margin<sup>(1)</sup> and gross margin as a percentage of revenue<sup>(1)</sup> for the year ended December 31, 2009 were \$19.5 million and 17% respectively, compared to \$29.8 million and 23% for the same period ended December 31, 2008.
- EBITDAS<sup>(1)</sup> for the year ended December 31, 2009 was \$10.0 million, compared to \$18.8 million for the year ended December 31, 2008.
- As at December 31, 2009, the Trust had total long-term debt of \$16.6 million compared to total long-term debt of \$17.5 million as at December 31, 2008. Long-term debt net of cash as at December 31, 2009 was \$15.5 million.
- The Trust's working capital in excess of long-term debt<sup>(1)</sup>, as at December 31, 2009 was \$9.0 million compared to \$10.8 million as at December 31, 2008.

The operating results for the year ended December 31, 2009 are generally not comparable to the results for 2008 due to the increased size, scope and geographical reach of the operations from the Builders acquisition and the completion of the divestiture of the Transport division. After giving consideration to these two transactions, only about one third of the current operations of the Trust are included in the first three months of operations of the Trust's comparative financial information in 2008.

**RESULTS OF OPERATIONS**

| (Thousands, except per unit amounts)   | Three months ended<br>December 31, |             | Year ended<br>December 31, |             |
|--|------------------------------------|-------------|----------------------------|-------------|
|  | 2009                               | 2008        | 2009                       | 2008        |
| Revenue  | \$ 30,108                          | \$ 43,842   | \$ 111,722                 | \$ 127,924  |
| Operating expenses   | 23,344                             | 31,756      | 92,243                     | 98,132      |
| Gross margin <sup>(1)</sup>  | 6,764                              | 12,086      | 19,479                     | 29,792      |
| Gross margin as a percentage of revenue <sup>(1)</sup>                                       | 22%                                | 28%         | 17%                        | 23%         |
| General and administrative expenses  | 2,178                              | 3,867       | 9,458                      | 10,991      |
| EBITDAS <sup>(1)</sup>   | 4,586                              | 8,219       | 10,021                     | 18,801      |
| EBITDAS as a percentage of revenue <sup>(1)</sup>  | 15%                                | 19%         | 9%                         | 15%         |
| Unit-based compensation  | 270                                | 361         | 1,214                      | 1,588       |
| Depreciation and amortization  | 5,266                              | 4,842       | 20,156                     | 17,427      |
| Interest on long-term debt   | 212                                | 289         | 1,230                      | 2,861       |
| Loss on disposal of assets   | 50                                 | 412         | 4,107                      | 610         |
| Earnings (loss) from continuing operations<br>before impairment of goodwill and income taxes | (1,212)                            | 2,315       | (16,686)                   | (3,685)     |
| Impairment of goodwill   | -                                  | 17,902      | -                          | 17,902      |
| Loss from continuing operations<br>before income taxes                                       | (1,212)                            | (15,587)    | (16,686)                   | (21,587)    |
| Future income tax expense (recovery)   | 197                                | (902)       | (7,206)                    | 1,856       |
| Loss from continuing operations  | (1,409)                            | (14,685)    | (9,480)                    | (23,443)    |
| Earnings (loss) from discontinued operations   | -                                  | (1,265)     | -                          | 4,182       |
| Net loss   | \$ (1,409)                         | \$ (15,950) | \$ (9,480)                 | \$ (19,261) |
| Net loss per unit<br>– basic and diluted   | \$ (0.02)                          | \$ (0.27)   | \$ (0.16)                  | \$ (0.36)   |

**Revenue**

| (Thousands)        | Three months ended<br>December 31, |           | Year ended<br>December 31, |            |
|--------------------|------------------------------------|-----------|----------------------------|------------|
|                    | 2009                               | 2008      | 2009                       | 2008       |
| Revenue            |                                    |           |                            |            |
| Well Servicing     | \$ 20,195                          | \$ 31,135 | \$ 72,415                  | \$ 95,970  |
| Wireline & Rentals | 9,913                              | 12,707    | 39,307                     | 31,954     |
|                    | \$ 30,108                          | \$ 43,842 | \$ 111,722                 | \$ 127,924 |

Revenue for the year ended December 31, 2009 was \$111.7 million, compared to \$127.9 million for the same period in 2008. Revenue for the three months ended December 31, 2009 was \$30.1 million, compared to \$43.8 million for the same period in 2008.

Comparative fleet information is as follows:

|                            | As at December 31, |      |
|----------------------------|--------------------|------|
|                            | 2009               | 2008 |
| Well Servicing Equipment*: |                    |      |
| Service Rigs               | 51                 | 53   |
| Rod Rigs                   | 23                 | 27   |
| Coil Tubing Rigs**         | 29                 | 32   |
| Wireline Equipment:        |                    |      |
| E-line Trucks              | 14                 | 13   |
| Slickline Trucks           | 6                  | 7    |

\* In addition to the fleet of service rigs, rod rigs and coil tubing rigs, Essential provides ancillary services through nitrogen pumpers, a cement & acid unit and other specialty equipment.

\*\* An intermediate Coil Tubing Rig was acquired and put into service in the first quarter of 2010 and is not included in the above count.

### Well Servicing

Essential provides well completion and production/workover services across western Canada through its fleet of service rigs, rod rigs and coil tubing rigs. Well Servicing generated revenue of \$72.4 million for the year ended December 31, 2009, compared to \$96.0 million for the same period in 2008. Well Servicing generated revenue of \$20.2 million for the three months ended December 31, 2009, compared to \$31.1 million for the same period in 2008.

Activity levels for Essential, and within the entire WCSB, were impacted during 2009 by reduced vertical conventional drilling, especially in Alberta where the majority of the Trust's services operate. Low commodity prices and reduced drilling, completions and well maintenance expenditures by exploration and production companies were the predominant factors behind the low activity levels during the year. Surplus industry equipment and declining activity levels have increased price competition and eroded margins during the year.

Comparative utilization of the well servicing fleet is as follows:

|                       | Three months ended<br>December 31, |      | Year ended<br>December 31, |      |
|-----------------------|------------------------------------|------|----------------------------|------|
|                       | 2009                               | 2008 | 2009                       | 2008 |
| Essential Utilization |                                    |      |                            |      |
| Service Rigs          | 34%                                | 47%  | 27%                        | 48%  |
| Rod Rigs              | 35%                                | 42%  | 32%                        | 48%  |
| Coil Tubing Rigs      | 37%                                | 51%  | 32%                        | 41%  |

Service rig utilization was well below historical levels throughout 2009. Low commodity prices and adverse credit markets caused many exploration and production companies to curtail their capital programs before the end of the first quarter of 2009 leading to an earlier decline in activity levels. During the summer months, faced with declining activity levels and pricing pressure, the Trust elected to accept lower utilization in certain situations rather than work at prices that were uneconomic. By the end of the fourth quarter, the Trust saw an improvement in activity levels for service rigs as improved natural gas prices and increased availability of credit enabled exploration and production companies to increase drilling and completion activities.

Higher activity levels on the shale plays in the Bakken region provided the Trust opportunities for coil tubing rigs given their ability to work on horizontal wells. The Trust had success redirecting some of its coil tubing fleet into Saskatchewan and B.C. where activity levels were less impacted by the downturn. In addition, the Trust increased the service and depth capacity of its coil tubing fleet with the introduction of a deep coil tubing rig during the latter half of the third quarter. Capable of reaching depths up to 3,750 meters while accommodating coil tubing up to 2" in diameter and depths up to 5,100 meters while using smaller diameter coil tubing, the deep coil tubing rig is ideally suited to work in the deep horizontal wells, generally found in the Bakken and Montney resource plays, as well as in the deeper Alberta plays.

Activity levels for Essential's coil tubing rigs remained strong during the fourth quarter as shale gas activity continued to be the focus of many exploration and production companies.

While utilization and revenue levels in the fourth quarter were down in comparison to the prior year, declines were less severe than anticipated. The fourth quarter started off slowly, continuing the trend of low activity levels experienced during the third quarter, but improved as the quarter progressed as exploration and production companies began their winter drilling programs in November and continued activity through to the end of December. Essential was able to overcome the labour challenges created from the improved activity levels through the steps that were taken in the earlier part of the year that enabled the Trust to retain quality personnel in this difficult labour market.

### **Wireline & Rentals**

Essential offers both electric wireline ("e-line") and slickline services, in addition to its downhole tool and equipment rental operations, through the Wireline & Rentals business segment. Wireline & Rentals generated revenue of \$39.3 million for the year ended December 31, 2009, compared to \$32.0 million for the same period in 2008 (prior to the completion of the Builders transaction in April 2008, the Trust did not operate a Wireline & Rentals segment). Wireline & Rentals generated revenue of \$9.9 million for the three months ended December 31, 2009, compared to \$12.7 million for the same period in 2008.

Within Essential's Wireline & Rentals segment, the downhole tool operations were a focused area of growth in 2009. During the year, the Trust expanded its service offerings and introduced multi-stage fracturing service which enables companies to stimulate horizontal wells, like those in the Bakken and Montney resource plays, in a more cost effective manner. The growth in the tool operations helped offset the decline in the Trust's tubular and pipe rentals business, which primarily offers products related to conventional oil and gas drilling activity. The growth in the tool operations also helped offset declines in the Trust's e-line business, where reduced activity in the shallow gas plays in Alberta and the competitive market for these services, because of a surplus of equipment in this service line, resulted in extreme pricing pressure.

Through the fourth quarter, the downhole tool operations continued to be a stabilizing presence in this segment while results for the e-line business continued to be impacted by extremely competitive market conditions. Activity in the Trust's tubular and pipe rental business, while lower than the prior year, improved over recent quarters as a result of the increased drilling and completion work during the quarter.

### **Operating Expenses**

| (Thousands)        | Three months ended<br>December 31, |           | Year ended<br>December 31, |           |
|--------------------|------------------------------------|-----------|----------------------------|-----------|
|                    | 2009                               | 2008      | 2009                       | 2008      |
| Operating expenses | \$ 23,344                          | \$ 31,756 | \$ 92,243                  | \$ 98,132 |
| As a % of revenue  | 78%                                | 72%       | 83%                        | 77%       |

Operating expenses were \$92.2 million for the year ended December 31, 2009, compared to \$98.1 million for the same period in 2008. Operating expenses were \$23.3 million for the three months ended December 31, 2009, compared to \$31.8 million for the same period in 2008.

Operating costs, including repairs and maintenance, fuel and certain labour costs, fluctuate in proportion to activity levels. Other operating costs, including costs associated with retaining key personnel, qualified equipment operators, maintaining service locations and insurance, are relatively fixed in nature and must be changed in steps in relation to a longer term industry outlook. During periods of decreased activity, operating costs as a percentage of revenue will increase due to the fixed nature of certain operating costs.

The Trust was proactive in managing its costs during the year based on current and anticipated activity. During the first three months of 2009, the Trust implemented significant cost reduction measures including staff reductions, unpaid leaves of absence, wage rollbacks and the suspension of the Trust's short term incentive program in order to preserve operating margins and remain competitive in future

periods. The Trust implemented further cost reductions throughout the year in an effort to continue to improve its cost structure. The Trust realized approximately \$6 million in operating cost savings in 2009 as a result of the cost reduction measures implemented throughout the year.

### General and Administrative Expenses

| (Thousands)                         | Three months ended<br>December 31, |          | Year ended<br>December 31, |           |
|-------------------------------------|------------------------------------|----------|----------------------------|-----------|
|                                     | 2009                               | 2008     | 2009                       | 2008      |
| General and administrative expenses | \$ 2,178                           | \$ 3,867 | \$ 9,458                   | \$ 10,991 |
| As a % of revenue                   | 7%                                 | 9%       | 8%                         | 9%        |

General and administrative expenses were \$9.5 million for the year ended December 31, 2009, compared to \$11.0 million for the same period in 2008. General and administrative expenses were \$2.2 million for the three months ended December 31, 2009, compared to \$3.9 million for the same period in 2008. These costs are comprised of wages, professional fees, office space and other administrative costs incurred at the corporate and business unit level.

In response to the deterioration of utilization levels and market conditions, management implemented cost reduction measures in early 2009 in an effort to reduce general and administrative costs. These measures included a 10% voluntary salary rollback for the executive management team, suspension of the Trust's short term incentive plan and savings plan programs, certain employees agreeing to take unpaid leaves of absence and headcount reductions. As a result of these initiatives, and other discretionary cost saving measures implemented since that time, the Trust realized approximately \$4 million of general and administrative cost savings throughout 2009.

### Unit-based Compensation Expense

The Trust recorded a non-cash expense related to unit-based compensation for the year ended December 31, 2009 of \$1.2 million, compared to \$1.6 million for the same period in 2008. The Trust recorded a non-cash expense related to unit-based compensation for the three months ended December 31, 2009 of \$0.3 million, compared to \$0.4 million for the same period in 2008. The decrease over the prior year expense is primarily due to forfeitures of options by departed employees and new grants being issued at lower fair values than forfeited grants.

### Depreciation and Amortization

| (Thousands)                   | Three months ended<br>December 31, |          | Year ended<br>December 31, |           |
|-------------------------------|------------------------------------|----------|----------------------------|-----------|
|                               | 2009                               | 2008     | 2009                       | 2008      |
| Depreciation and amortization | \$ 5,266                           | \$ 4,842 | \$ 20,156                  | \$ 17,427 |

Depreciation and amortization expense was \$20.2 million for the year ended December 31, 2009, compared to \$17.4 million for the same period in 2008. Depreciation and amortization expense was \$5.3 million for the three months ended December 31, 2009, compared to \$4.8 million for the same period in 2008. The increase in the yearly depreciation is due to the increase in the size and nature of the equipment fleet resulting from the acquisition of Builders.

**Interest on Long-term Debt**

| (Thousands)                | Three months ended<br>December 31, |        | Year ended<br>December 31, |          |
|----------------------------|------------------------------------|--------|----------------------------|----------|
|                            | 2009                               | 2008   | 2009                       | 2008     |
| Interest on long-term debt | \$ 212                             | \$ 289 | \$ 1,230                   | \$ 2,861 |
| Average interest rate      | 3.6%                               | 4.1%   | 3.3%                       | 5.7%     |

Interest expense was \$1.2 million for the year ended December 31, 2009, compared to \$2.9 million for the same period in 2008. Interest expense was \$0.2 million for the three months ended December 31, 2009, compared to \$0.3 million for the same period in 2008. Interest expense for the year ended December 31, 2009 includes fees related to the renewal of the Trust's credit facility.

Interest on long-term debt has declined in the three months and year ended December 31, 2009 in comparison to the same periods in 2008, due to the significantly lower average long-term debt outstanding during the period combined with lower interest rates. The average long-term debt outstanding for the three months and year ended December 31, 2009 was \$16.3 million and \$15.4 million, respectively, in comparison to an average of \$20.7 million and \$66.9 million, respectively, for the same periods ended December 31, 2008. Essential's low debt continues to provide the Trust with a competitive advantage, not only because of available credit, but also due to reduced interest costs on an ongoing basis.

**Income Taxes**

| (Thousands)                          | Three months ended<br>December 31, |          | Year ended<br>December 31, |          |
|--------------------------------------|------------------------------------|----------|----------------------------|----------|
|                                      | 2009                               | 2008     | 2009                       | 2008     |
| Future income tax expense (recovery) | \$ 197                             | \$ (902) | \$ (7,206)                 | \$ 1,856 |

Future income tax recovery was \$7.2 million for the year ended December 31, 2009, compared to future income tax expense of \$1.9 million for the same period in 2008. Future income tax expense was \$0.2 million for the three months ended December 31, 2009, compared to future income tax recovery of \$0.9 million for the same period in 2008.

In June 2007, the Government of Canada enacted legislation imposing additional income taxes on trusts for taxation years commencing January 1, 2011. The Trust is subject to income taxes based on the temporary differences expected to be in effect at January 1, 2011. Changes in the current period result from changes in these expectations.

The Trust does not anticipate current taxes prior to 2011 as its tax pools should be sufficient to shelter any taxable income during those periods.

In November 2008, the Government of Canada enacted legislation to permit a trust to convert to a corporation. The legislation proposes to reduce the administration and compliance associated with a conversion and to allow for the tax deferred conversion of a trust to a corporation. In November 2009, the Trust announced its intention to convert to a growth-oriented corporation prior to April 30, 2010 pursuant to a Plan of Arrangement under the Business Corporations Act (Alberta).

**Impairment of Goodwill**

| (Thousands)            | Three months ended<br>December 31, |           | Year ended<br>December 31, |           |
|------------------------|------------------------------------|-----------|----------------------------|-----------|
|                        | 2009                               | 2008      | 2009                       | 2008      |
| Impairment of goodwill | \$ -                               | \$ 17,902 | \$ -                       | \$ 17,902 |

Impairment of goodwill for the three months and year ended December 31, 2009 was \$nil, compared to \$17.9 million for the same periods ended December 31, 2008. Following the recognition of the impairment on goodwill in 2008, the Trust no longer has any goodwill recorded on its Balance Sheet.

**SUMMARY OF QUARTERLY DATA**

| (\$Thousands, except<br>per unit amounts)           | Dec 31,<br>2009 | Sep 30,<br>2009 | Jun 30,<br>2009 | Mar 31,<br>2009 | Dec 31,<br>2008 | Sep 30,<br>2008 | Jun 30,<br>2008 | Mar 31,<br>2008 |
|---|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|
| Revenue from continuing operations                  | 30,108          | 23,442          | 15,974          | 42,198          | 43,842          | 43,891          | 25,145          | 15,046          |
| Net earnings (loss)                                 | (1,409)         | (2,661)         | (10,972)        | 5,562           | (15,950)        | 8,400           | (14,424)        | 2,713           |
| Per unit – basic and diluted                        | (0.02)          | (0.04)          | (0.18)          | 0.09            | (0.27)          | 0.14            | (0.24)          | 0.08            |
| Funds flow from (used) in Operations <sup>(1)</sup> | 4,374           | 615             | (3,983)         | 7,785           | 6,113           | 8,122           | (5,361)         | 7,109           |
| Per unit – basic and diluted                        | 0.07            | 0.01            | (0.07)          | 0.13            | 0.09            | 0.13            | (0.10)          | 0.20            |
| Distributions per unit                              | -               | 0.01            | 0.01            | 0.03            | 0.04            | 0.05            | 0.12            | 0.15            |

Quarterly data only incorporates the impact of the Builders acquisition for the quarters ended subsequent to March 31, 2008. Net earnings (loss) for the period ended December 31, 2008 includes a goodwill impairment charge of \$17.9 million.

**FINANCIAL RESOURCES AND LIQUIDITY**

In light of the prolonged downturn in the oilfield services sector, and in order to preserve its balance sheet, the Trust announced in November 2009 the elimination of its distribution and its plans to convert to a growth-oriented corporation, pursuant to a Plan of Arrangement under the Business Corporations Act (Alberta), by April 30, 2010. This decision will enable the Trust to redirect future expected funds flow from operations to maintaining the working capacity of its fleet and to pursue future growth initiatives. Prior to the elimination of the distribution, the Board of Directors of the Trust reviewed and approved the distribution level and paid distributions on a monthly basis for 2008 and the first quarter of 2009 and on a quarterly basis for the second and third quarters of 2009.

**Funds Flow from Operations<sup>(1)</sup>**

| (Thousands)  | Three months ended<br>December 31, |           | Year ended<br>December 31, |           |
|--|------------------------------------|-----------|----------------------------|-----------|
|  | 2009                               | 2008      | 2009                       | 2008      |
| Cash flow from operations                              | \$ 269                             | \$ 11,568 | \$ 15,108                  | \$ 37,183 |
| Less:  |                                    |           |                            |           |
| Non-cash operating working capital increase (decrease) | 4,105                              | (5,455)   | (6,317)                    | (21,196)  |
| Funds flow from operations                             | \$ 4,374                           | \$ 6,113  | \$ 8,791                   | \$ 15,987 |
| Per unit – basic and diluted                           | \$ 0.07                            | \$ 0.10   | \$ 0.15                    | \$ 0.30   |

Funds flow from operations<sup>(1)</sup> was \$8.8 million for the year ended December 31, 2009, compared to \$16.0 million for the same period in 2008. Funds flow from operations<sup>(1)</sup> was \$4.4 million for the three months ended December 31, 2009, compared to \$6.1 million for the same period in 2008.

### Working Capital

| (Thousands)  | December 31,<br>2009 | December 31,<br>2008 |
|--|----------------------|----------------------|
| Current assets   | \$ 35,026            | \$ 44,360            |
| Current liabilities, excluding current portion of long-term debt | (9,413)              | (16,062)             |
| <b>Working capital</b>   | <b>\$ 25,613</b>     | <b>\$ 28,298</b>     |
| <b>Working capital ratio</b>                                     | <b>3.7:1</b>         | <b>2.8:1</b>         |

Working capital at December 31, 2009 was \$25.6 million compared to \$28.3 million at December 31, 2008. Working capital declined as a result of reduced activity levels in 2009 compared to the prior year.

### Working Capital Net of Long-term Debt

| (Thousands)   | December 31,<br>2009 | December 31,<br>2008 |
|---|----------------------|----------------------|
| Working capital   | \$ 25,613            | \$ 28,298            |
| Long-term debt, including the current portion of long-term debt | (16,600)             | (17,525)             |
| <b>Working capital net of long-term debt</b>                    | <b>\$ 9,013</b>      | <b>\$ 10,773</b>     |

Working capital exceeded long-term debt at December 31, 2009 by \$9.0 million compared to \$10.8 million at December 31, 2008. Notwithstanding the sharp decline in activity levels in 2009, the Trust was able to preserve a strong working capital position through proactive cash flow management initiatives during the year.

### Credit Facility

The Trust's credit agreement with its banking syndicate is comprised of an extendible revolving loan facility (the "Facility"). The Trust renewed its credit facility with the existing banking syndicate on May 30, 2009. At management's request, the facility size was reduced at the time of renewal in May 2009 from \$140 million to \$50 million to minimize standby and renewal fees. In addition, the Facility was amended to add a \$25 million accordion feature that may be exercised at a future date, subject to certain terms and conditions.

Under the agreement, the Facility is limited to the lesser of \$50 million or the sum of 75% of the Trust's accounts receivables less specific items (the "Borrowing Base") and 60% of the Trust's carrying value of property and equipment less term debt. The Borrowing Base must be at least 20% of the Facility otherwise the Facility is reduced by the amount of any shortfall. At December 31, 2009, a maximum of \$50 million was available to the Trust. The Facility has no required principal repayments until expiry and bears interest that fluctuates with the bank's prime rate or bankers' acceptance rate plus a margin based on financial covenants. On March 10, 2010, \$17.4 million of long-term debt was outstanding.

The Facility expires on May 30, 2010 and can be renewed, at the syndicate's option upon request by the Trust. If not renewed, debt repayments would be made monthly over a two year period, based on a three year amortization schedule.

As at December 31, 2009, all financial debt covenants were satisfied and all banking requirements were up to date. The Trust does not anticipate any financial resources or liquidity issues to restrict its future operating, investing or financing activities.

**Equipment Expenditures**

| (Thousands)  | Three months ended<br>December 31, |          | Year ended<br>December 31, |           |
|--|------------------------------------|----------|----------------------------|-----------|
|  | 2009                               | 2008     | 2009                       | 2008      |
| Equipment expenditures                                 |                                    |          |                            |           |
| Well Servicing   | \$ 247                             | \$ 3,726 | \$ 5,641                   | \$ 7,816  |
| Wireline & Rentals                                     | 204                                | 3,220    | 1,370                      | 5,289     |
| Corporate  | 172                                | 392      | 822                        | 864       |
|  | <b>623</b>                         | 7,338    | <b>7,833</b>               | 13,969    |
| Less proceeds on disposal of property<br>and equipment | (66)                               | (719)    | (473)                      | (1,619)   |
| Net equipment expenditures <sup>(1)</sup>              | \$ 557                             | \$ 6,619 | \$ 7,360                   | \$ 12,350 |

Net equipment expenditures<sup>(1)</sup> for the year ended December 31, 2009 were \$7.4 million compared to \$12.4 million for the same period ended December 31, 2008. Net equipment expenditures<sup>(1)</sup> for the three months ended December 31, 2009 were \$0.6 million compared to \$6.6 million for the same period ended December 31, 2008.

Essential classifies its equipment expenditures as growth capital and maintenance capital, which includes information systems, operational facilities and leasehold improvements. Comparative equipment expenditures are as follows:

| (Thousands)            | Three months ended<br>December 31, |          | Year ended<br>December 31, |           |
|------------------------|------------------------------------|----------|----------------------------|-----------|
|                        | 2009                               | 2008     | 2009                       | 2008      |
| Equipment expenditures |                                    |          |                            |           |
| Growth capital         | \$ 176                             | \$ 5,214 | \$ 4,894                   | \$ 8,808  |
| Maintenance capital    | 447                                | 2,124    | 2,939                      | 5,161     |
|                        | \$ 623                             | \$ 7,338 | \$ 7,833                   | \$ 13,969 |

In light of current industry conditions and the outlook for 2010, the Trust has established a conservative 2010 capital spending budget of \$6.2 million comprised of \$1.8 million of growth capital and \$4.4 million of net maintenance capital.

Essential will continue to assess the appropriate level of capital spending relative to industry activity and opportunities throughout 2010.

**Trust Units**

As at March 10, 2010, there were 59,852,965 Trust units and 5,263,416 Trust unit options outstanding (including 293,083 Essential Replacement Options issued in conjunction with the acquisition of Builders). Of the 5,263,416 Trust unit options, 1,742,317 were exercisable of which 412,324 were "in-the-money".

**NORMAL COURSE ISSUER BID ("NCIB")**

On October 29, 2008 the Trust received approval from the Toronto Stock Exchange ("TSX") to implement an NCIB commencing on October 31, 2008 and terminating on October 30, 2009. Purchases were made at the discretion of management at prevailing market prices, through the facilities of the TSX. The Trust acquired and cancelled no units during the year ended December 31, 2009 (2008 - 419,000 units at a cost of \$0.4 million with \$1.4 million transferred to contributed surplus upon the share cancellations).

The NCIB expired on October 30, 2009, and the Trust did not renew it.

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**DISCLOSURE CONTROLS AND PROCEDURES**

The Trust's Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO") have designed, or caused to be designed under their supervision, disclosure controls and procedures to provide reasonable assurance that: (i) material information relating to the Trust is made known to the Trust's CEO and CFO by others, particularly during the period in which annual filings are being prepared; and (ii) information required to be disclosed by the Trust in its annual filings, interim filings or other reports filed or submitted by it under securities legislation is recorded, processed, summarized and reported within the time period specified in securities legislation. Such officers have evaluated, or caused to be evaluated under their supervision, the effectiveness of the Trust's disclosure controls and procedures at the financial year end of the Trust and have concluded that the Trust's disclosure controls and procedures are effective at the financial year end of the Trust for the foregoing purposes.

**INTERNAL CONTROLS OVER FINANCIAL REPORTING**

Internal controls over financial reporting are designed to provide reasonable assurance regarding the reliability of the Trust's financial reporting and the preparation of financial statements together with the other financial information for external purposes in accordance with GAAP. The Trust's CEO and CFO are responsible for designing, or causing to be designed under their supervision, internal controls over financial reporting related to the Trust, including its consolidated subsidiaries.

During the year, the Trust's management under the supervision of and with the participation of its CEO and CFO completed an assessment on the design and effectiveness of internal control over financial reporting. In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO") in Internal Control – Integrated Framework. The assessment includes a risk-based evaluation and documentation and testing of key processes. All internal control systems, no matter how well designed, have inherent limitations. Therefore, these systems provide reasonable, but not absolute assurance, that disclosures and financial information is accurate and complete.

Through management's assessment of the design and effectiveness of internal controls over financial reporting, no material weaknesses were found. The broad scope of senior management's oversight and strong entity level controls are expected to compensate for any non-material control weaknesses. In addition, non-material control weaknesses identified are mitigated by the active involvement of senior management in all the affairs of the Trust; open lines of communication within the Trust and its divisions; the present levels of activities and transactions within the Trust being readily transparent; the thorough review of the Trust's financial statements by management; and the existence of a whistle-blower policy.

The Trust's CEO and CFO have concluded, based on their evaluation as of the end of the period covered by the Trust's annual filings for the year ended December 31, 2009, that the Trust's internal control over financial reporting, as defined in National Instrument 52-109, are operating effectively and are suitably designed to provide reasonable assurance regarding the reliability of the Trust's financial reporting and the preparation of financial statements together with the other financial information for external purposes in accordance with Canadian GAAP.

**CRITICAL ACCOUNTING ESTIMATES**

Preparation of consolidated financial statements requires that the Trust make assumptions regarding accounting estimates for certain amounts contained within the consolidated financial statements. The Trust's significant accounting estimates include net realizable value of inventory; depreciation of property and equipment; the fair value of assets and liabilities acquired in business combinations; estimated impairment of long-lived assets; estimated intangible assets; goodwill impairment; estimated fair value calculations of unit based compensation; estimates used in the determination of current and future tax provisions; and estimating bad debts on accounts receivable. In light of the current economic conditions, the Trust believes it has been conservative in its assumptions regarding accounting estimates. The Trust believes that each of the assumptions and estimates is appropriate to the circumstances and represents the most likely future outcome. However, because of the uncertainties inherent in making assumptions and estimates regarding unknown future outcomes, future events may result in significant differences between estimates and actual results.

**Provision for Doubtful Accounts Receivable**

The Trust performs periodic credit evaluations of its customers and grants credit based upon past payment history, financial condition, and anticipated industry conditions. Customer payments are regularly monitored and a provision for doubtful accounts is established based upon specific situations and overall industry conditions. The history of bad debt losses of the trust has been within expectations and is generally limited to specific customer circumstances. However, given the cyclical nature of the energy industry, a customer's ability to fulfill its payment obligations can change suddenly and without notice.

**Depreciation and Amortization**

The equipment of the Trust is depreciated based upon its estimated useful lives and salvage values. For intangible assets, the amortization policies selected are intended to amortize the assets over their expected lives or contracted terms. The Trust reviews its historical experience with similar assets to help ensure that these depreciation and amortization rates are appropriate. However, the actual useful life of the assets may differ from the original estimate due to factors such as technological obsolescence and maintenance activity.

**Impairment of Long-lived Assets**

The Trust assesses the carrying value of long-lived assets, which include property and equipment, intangible assets and goodwill, for indications of impairment when events or circumstances indicate that the carrying amounts may not be recoverable from estimated cash flows. Estimating future cash flows requires assumptions about future business conditions and technological developments. Significant, unanticipated changes to these assumptions could require a provision for impairment in the future.

**Unit-based Compensation**

Unit-based compensation is provided in respect of the unit option plan. The expense is calculated using the fair value method based upon the Black-Scholes model. In order to establish fair value the Trust uses estimates and assumptions to determine risk-free interest rate, expected term, anticipated volatility and distribution yield.

**Fair Value of Assets and Liabilities Acquired in Business Combinations**

The value of acquired assets and liabilities on the acquisition date require the use of estimates to determine the purchase price allocation. Estimates are made as to the valuations of property and equipment, intangible assets, and goodwill, among other items. In certain circumstances, such as the valuation of property and equipment acquired, the Trust may rely on independent third party valuations.

**ACCOUNTING POLICIES**

During the year ended December 31, 2009, Essential adopted three new accounting standards that were issued by the Canadian Institute of Chartered Accountants ("CICA"): Handbook Section 3064 "Goodwill and Intangible Assets", Handbook Section 3862 "Financial Instruments — Disclosures" and EIC 173 "Credit Risk and the Fair Value of Financial Assets and Financial Liabilities".

**Goodwill and Intangible Assets**

This section establishes the standards for the recognition, measurement, presentation and disclosure of goodwill subsequent to its initial recognition and of intangible assets by profit-oriented enterprises. This standard has been adopted effective January 1, 2009. Essential has assessed the impact of this standard and noted no impact to its intangible assets.

**Credit Risk and the Fair Value of Financial Assets and Financial Liabilities**

This EIC impacts the application of Section 3855 "Financial Instruments – Recognition and Measurement". This EIC outlines the inclusion of an entity's credit risk and the credit risk of counterparties in the determination of fair value of financial assets and liabilities. The treatment outlined

in this EIC is to be applied retroactively without restatement effective January 20, 2009. This standard was adopted effective January 20, 2009. The Trust has assessed the impact of this standard and noted no impact to its financial statements.

#### **Financial Instruments — Disclosures**

This section outlines the criteria under which the fair value of financial instruments is recognized and measured. In June 2009, the CICA issued amendments to Section 3862. The standard expands disclosure requirements regarding the reliability of the inputs used in the measurement of financial instruments. The section has also been amended to require disclosure of the three levels of fair value hierarchy for the recognized financial instruments as well as additional liquidity disclosures. Adoption of this standard did not have an impact on the financial position or the results of operations of the Trust except for additional disclosure.

#### **Recent accounting pronouncements**

The following new accounting standards issued by the Canadian Institute of Chartered Accountants ("CICA") are not yet effective but are applicable to the Trust's future reporting periods.

#### **Business Combinations, Consolidated Financial Statements and Non-Controlling Interests**

In January 2009, as part of the convergence of Canadian GAAP with IFRS, the AcSB issued Section 1582 – Business Combinations, Section 1601 – Consolidated Financial Statements and Section 1602 – Non-controlling interests. These standards are to be adopted prospectively for fiscal years beginning on or after January 1, 2011 and early adoption is permitted. These standards provide the Canadian equivalent to IFRS standards.

#### **INTERNATIONAL FINANCIAL REPORTING STANDARDS ("IFRS")**

In 2008, the Canadian Accounting Standards Board (AcSB) confirmed that publicly accountable enterprises will be required to adopt International Financial Reporting Standards ("IFRS"), for interim and annual reporting purposes, beginning on or after January 1, 2011. The adoption date of January 1, 2011 will require the restatement, for comparative purposes, of amounts reported by the Trust for its year ended December 31, 2010, and of the opening balance sheet as at January 1, 2010.

The two key elements of the project plan are: financial statement compliance with IFRS and the business impact resulting from the conversion to IFRS. Financial statement compliance with IFRS consists of four phases as discussed in the following table. The business impact element of the project will ensure that companies consider, on a timely basis, the implication of any prospective change in accounting standards on other areas of the business. This includes, but is not limited to, information system infrastructure and processes, business agreements and financing arrangements, key metrics and the control environment.

Essential commenced its IFRS conversion project in 2008. The project plan consists of four phases: the impact assessment, design and planning, solution development and implementation. The Trust has completed the initial assessment phase which included a high level review of the major differences between current Canadian GAAP and IFRS, and an initial evaluation of IFRS 1 transition exemptions. The Trust has also completed the design and planning phase which included in depth research of the specific differences between current Canadian GAAP and IFRS, transitional options available and identification of potential implications on the existing policies and processes.

| Financial Statement Compliance with IFRS   | Milestones/Deadlines |
|--|----------------------|
| <ul style="list-style-type: none"> <li>Impact assessment phase - Initial identification of the major differences between current Canadian GAAP and IFRS standards and assessment of the impact of these differences in terms of the complexity of implementation and prospective timelines.</li> </ul>   | Completed            |
| <ul style="list-style-type: none"> <li>Design and planning phase - Research specific differences between the standards, long-term and transitional options available and prospective changes to the IFRS standards prior to 2011. Identify potential implications on accounting policies and processes, business management, information systems, control environment and educational requirements. Develop a formal plan to meet project objectives.</li> </ul> | Completed            |
| <ul style="list-style-type: none"> <li>Solution development phase - Quantify and evaluate transitional and long-term options available and select the most appropriate policies.</li> </ul>  | In progress          |
| <ul style="list-style-type: none"> <li>Implementation phase - Integrate solutions into the underlying financial processes and systems.</li> </ul>  | In progress          |

The conversion project has been driven by the finance group with input from all other functional areas, including but not limited to: operations, investor relations, tax and compliance and information technology. The use of staff from all functional area to assess IFRS accounting policy options assists in generating appropriate recommendations and identifying the business implications throughout the project. The project plan has been designed with some flexibility to be able to adapt to unexpected developments as new accounting developments are made by the AcSB and the International Accounting Standards Board ("IASB") to ensure that Essential is fully compliant on adoption of IFRS. Updates have been provided to the audit committee on a quarterly basis.

The transition to IFRS requires the Trust to apply IFRS 1, "First-Time Adoption of International Financial Reporting Standards" ("IFRS 1") which details the requirements for preparing IFRS-compliant financial statements in the first reporting period after the date of transition (January 1, 2010). IFRS 1 provides entities adopting IFRS for the first time with a number of optional exemptions and mandatory exceptions in certain areas to the general requirement for full retrospective application of IFRS. Based on management's analysis of the various accounting policy choices available, the IFRS 1 elections relevant to Essential are as follows:

- Business Combinations – IFRS 1 would allow Essential to use the standards for business combinations under IFRS 3 on a prospective basis rather than re-stating all past business combinations.
- Leases – IFRS 1 would allow Essential to elect to apply the rules for leases under IFRS 17 on a prospective basis from the date of transition rather than reassessing all previous leases to determine if they would be considered finance leases under IFRS.
- Property, Plant and Equipment ("PP&E") – IFRS 1 would allow Essential to elect to have the fair value or revaluation amount as the deemed cost of PP&E at the date of transition. In accordance with IFRS 1, Essential may elect to measure certain items of PP&E at their fair values at the date of transition and is in the process of analyzing the data to determine the impact on opening retained earnings. Any fair value adjustments and changes to the assessment of the related useful lives of the individual components of PP&E could impact the depreciation charges subsequent to the date of transition.
- Share-Based Payments – IFRS 1 allows an exemption to IFRS 2, "Share-Based Payments" for equity instruments granted on or before November 2, 2002 or which vested before the transition date to IFRS.

The application of IFRS1 is anticipated to impact certain balances of Essential's opening consolidated balance sheet under IFRS. The Trust is in the process of analyzing the data and cannot quantify the magnitude of adjustments at this time.

At this time, Essential has identified several differences arising from the adoption of IFRS that may impact the financial statements:

- Presentation of financial information – IFRS requires the presentation of expenses recognized in profit or loss using a classification based on either their nature or their function within the entity. Essential uses a blended classification methodology in its current income statement that will have to be changed to comply with IFRS.
- Impairment of PP&E assets – Under IFRS, impairment of PP&E is calculated at a more granular level than what is currently required under Canadian GAAP. Additionally the assessment of impairment under IFRS is completed using a discounted cash flow method in comparison to the undiscounted cash flow method used under Canadian GAAP.
- Share-Based Payments – Under IFRS, awards that vest in installments over the life of the grant are required to be treated as separate grants which will result in a variance in the expense calculation associated with these grants.

The impact of the differences noted above is not quantifiable at this time and will be further assessed as the Trust continues its IFRS conversion. Additionally, the areas impacted by IFRS discussed above should not be regarded as a comprehensive list of changes that will result from the transition to IFRS. Essential continues to monitor the development of standards, which are expected to change prior to 2011.

During the solution development and implementation phases, the Trust will quantify and further evaluate the transitional and long-term options available to the Trust and implement the identified changes to business processes, financial systems, accounting policies, disclosure controls and procedures and internal controls over financial reporting.

## **RISKS AND UNCERTAINTIES**

### **General**

Certain activities of Essential are affected by factors that are beyond its control or influence. The oilfield services business is directly affected by fluctuations in the levels of exploration, oil and natural gas development and production activity carried on by its customers, which in turn is dictated by numerous factors, including world energy prices and government policies. Additionally, the business risks also include: seasonality, with typically lower second and third quarter and higher fourth and first quarter activity; availability of skilled workers; ability to retain key customers; and the environmental and safety risks inherent in the business.

### **Service Industry Conditions**

The oil and gas services sector is highly reliant on the levels of capital expenditures made by oil and natural gas companies. Exploration and production companies base their capital expenditures on several factors, including but not limited to hydrocarbon prices, production levels and access to capital. In recent years, commodity prices, and therefore, the level 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 Essential's services. A significant, prolonged decline in commodity prices could have a material adverse effect on the oilfield services sector, results of operations and financial condition. The price of fuel, equipment and other input costs, insurance costs, interest rates, fluctuations in customers' business cycles and international, national and regional economic conditions are factors over which Essential has little or no control. A prolonged decline in commodity prices and field activity or significant increases in fuel prices, equipment prices, other input prices, interest rates or insurance costs, could reduce profitability and could adversely affect Essential's cash flow. Essential cannot predict the impact of future economic conditions and there is no assurance that the operations of Essential will continue to be profitable.

**Seasonality of Operations**

In the WCSB, the level of activity in the oilfield services sector is influenced by seasonal weather patterns. Spring breakup during the second quarter leaves many secondary roads temporarily incapable of supporting the weight of heavy equipment, which results in restrictions in the level of oilfield services. The duration of this period has a direct impact on the level of Essential's activities. Spring breakup typically occurs earlier in the year in southern regions than it does in the northern regions. The timing and duration of spring breakup are dependent on weather patterns but generally begins in March and continues into April and May. Additionally, if an unseasonably warm winter prevents sufficient freezing, Essential may not be able to access certain well sites and its operating results and financial condition may be adversely affected.

The demand for oilfield services may also be affected by the severity of the Canadian winters. In addition, during excessively rainy periods, equipment moves may be delayed, thereby adversely affecting revenues. The volatility in the weather and temperature can therefore create unpredictability in activity and utilization rates, which can have a material adverse effect on Essential's business, financial condition, results of operations and cash flows.

**Alberta Royalties**

In Alberta, the Crown royalty rates on conventional oil and natural gas fluctuate, depending on when a well was drilled, well depth, well production volume and the price of oil and natural gas. On October 25, 2007 the Alberta Government introduced a new royalty regime which became effective on January 1, 2009 and is applicable to all existing conventional oil and natural gas wells in Alberta. The new royalty regime assesses the applicable royalty rate on a well by well basis using a sliding scale which takes into account the price of oil and/or natural gas and the well's production volumes.

On November 19, 2008 and November 24, 2008 the Alberta Government announced details of an optional five-year transitional royalty program ("Transitional Program"). The Transitional Program applies to conventional oil and natural gas wells drilled to measured depths between 1,000 to 3,500 meters between November 19, 2008 and January 1, 2014. For each well, the producer can make a one time election to produce the well under the old royalty regime or the new royalty regime. As of January 1, 2014 all production subject to the Transitional Program will revert to the new royalty regime.

In March 2009, the Alberta Government announced additional incentives and in June 2009 announced a competitiveness review of the royalty program. The results of the competitiveness review are expected to be released in 2010.

Essential believes the new royalty regime in Alberta had a negative impact on the exploration and production activity among oil and natural gas companies operating in Alberta. As Essential provides services and equipment to such companies, it is believed that the new royalty regime reduced the demand for the services and equipment provided by Essential. It is not possible at this time to determine the timing and impact of the competitiveness review which the government has indicated will be released in 2010.

**Other risk factors**

For additional information that could impact the Trust's business, see "Risk Factors" in the Trust's Annual Information Form which is available on SEDAR at [www.sedar.com](http://www.sedar.com).

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**OUTLOOK**

There are a number of indications that the cycle has bottomed and the oilfield services sector is emerging from the downturn. Activity levels to-date in 2010 are higher than activity levels in the first quarter of 2009 as the spending of the exploration and production companies has increased. Oil prices have stabilized and are significantly higher than a year ago and natural gas prices are ahead of where they were a year ago. However, the industry will continue to monitor natural gas storage levels which are currently around the 5-year average. There is also a feeling of hope in Alberta as the government is expected to complete their competitiveness review shortly and many are optimistic the decisions will stimulate activity in the province later in 2010.

Any optimism for 2010 must be kept in perspective as the various industry projections for well counts, while generally ahead of 2009, are still far behind the number of wells drilled in the recent past. In addition, pricing for services are lower than a year ago, impacting margins for many services.

In 2009 there were notable changes in the WCSB oil and natural gas industry which are expected to continue into 2010 including a shift from conventional vertical drilling to horizontal and directional drilling and increased interest in the Cardium and Viking plays in Alberta. Essential has been able to respond to these changes as its service rigs, coil tubing rigs and multi-stage fracturing services are capable of working on horizontal and directional wells and many of Essential's customers are becoming active in the Cardium and Viking plays.

Through the experience of the recent downturn, management and the Board has determined it is in the best interest of Essential to look beyond its traditional geographic boundaries and Essential is investigating expansion opportunities in Colombia. The Trust recently hired a Director of Business Development for Latin America and preliminary discussions suggest there may be opportunities to redeploy some of Essential's equipment and expertise to this region.

The initial capital spending program announced for 2010 is modest and is intended to preserve the operating capacity of the equipment fleet. If activity levels, market conditions and opportunities continue to improve the capital program will be increased to take advantage of opportunities for future growth. Possible areas of growth include coil tubing equipment for deeper Alberta plays and modifications to portions of the fleet to be suitable for Latin American operations. The Trust's balance sheet remained strong through 2009 and as industry activity increases, the flexibility that comes with Essential's financial position becomes a competitive advantage.

Essential is working towards the previously announced conversion to a growth-oriented corporation. Management intends to have it completed by the end of April 2010, subject to unitholder and regulatory approval. Removal of the uncertainty that exists in the income trust market today, with the looming January 2011 deadline before tax changes, and possible improved access to capital are among the reasons to convert.

In the past year Essential has proven its ability to take necessary measures to deal with challenging conditions. If activity does not continue to improve as anticipated, Essential will continue to benefit from the extensive cost reduction measures taken in 2009. If activity does increase later in the year, the skilled work force, equipment fleet and strong balance sheet should enable Essential to quickly respond to opportunities that may develop.

<sup>(1)</sup>Non-GAAP Measures

Throughout this MD&A, certain terms that are not specifically defined in Canadian Generally Accepted Accounting Principles ("GAAP") are used to analyze the operations. In addition to the primary measures of net earnings and net earnings per unit in accordance with GAAP, the Trust believes that certain measures not recognized under GAAP assist both the Trust and the reader in assessing performance and understanding the Trust's results. Each of these measures provides the reader with additional insight into the Trust's ability to fund future distributions, principal debt repayments and capital programs. These non-GAAP measures are not recognized measures under GAAP. As a result, the method of calculation may not be comparable with other companies or Trusts. These measures should not be considered alternatives to net earnings and net earnings per unit as calculated in accordance with GAAP.

Gross margin<sup>(2)</sup> – This measure is considered a primary indicator of operating performance as calculated by revenue less operating expenses.

Gross margin as a percentage of revenue<sup>(2)</sup> – This measure is considered a primary indicator of operating performance as calculated by gross margin divided by revenue.

EBITDAS<sup>(3)</sup> (Earnings before interest, income taxes, depreciation, amortization, non-controlling interest earnings, losses or gains on disposal of equipment, results of discontinued operations, impairment of goodwill and unit based compensation) – This measure is considered an indicator of the Trust's ability to generate funds flow in order to meet distributions, fund required working capital, service debt, pay current income taxes and fund capital programs.

EBITDAS as a percentage of revenue<sup>(3)</sup> – This measure is considered an indicator of the Trust's ability to generate funds flow as calculated by EBITDAS<sup>(3)</sup> divided by revenue.

Funds flow or funds flow from (used in) operations<sup>(4)</sup> – This measure is an indicator of the Trust's ability to generate funds flow<sup>(4)</sup> in order to fund distributions, working capital, principal debt repayments and capital programs. Funds flow or funds flow from operations is defined as cash flow from operations before changes in non-cash operating working capital. This measure is useful in assessing the Trust's operational cash flow as it provides cash generated in the period excluding the timing of non-cash operating working capital. This reflects the ability of the operations of the Trust to meet the above noted funding requirements.

Working capital in excess of long-term debt – This measure is considered an indicator of the financial strength of the Trust.

Growth capital – Growth capital is capital spending which is intended to result in incremental increases in revenue. Growth capital is considered to be a key measure as it represents the total expenditures on equipment expected to add incremental revenues and funds flow to the Trust.

Net maintenance capital – Equipment additions that are incurred in order to refurbish or replace previously acquired equipment less proceeds on the disposal of retired equipment. Such additions do not provide incremental increases in revenue. Net maintenance capital is a key component in understanding the sustainability of the Trust's business as cash resources retained within the Trust must be sufficient to meet net maintenance capital needs to replenish the assets for future cash generation.

Net equipment expenditures<sup>(5)</sup> – This measure is equipment expenditures less proceeds on the disposal of equipment. The Trust uses net equipment expenditures to assess net cash flows related to the financing of the Trust's oilfield services equipment.

<sup>2</sup> Gross margin and gross margin as a percentage of revenue are reconciled to the GAAP measures, revenue and operating costs, in the table "Results of Operations".

<sup>3</sup> EBITDAS and EBITDAS as a percentage of revenue are reconciled to the GAAP measure, loss from continuing operations before income taxes, in the table "Results of Operations".

<sup>4</sup> Funds flow is reconciled to the GAAP measure, cash flow from operations, in the table "Funds Flow from Operations".

<sup>5</sup> Net equipment expenditures is calculated from the GAAP measures, equipment expenditures and proceeds on disposal of equipment, in the table "Equipment Expenditures"

## **C O R P O R A T E I N F O R M A T I O N**

### **Directors**

James A. Banister<sup>2,3</sup>, Chairman

Garnet K. Amundson

Michael J. Black<sup>2</sup>

Verne G. Johnson<sup>1,3</sup>

Nicholas G. Kirton<sup>1,2</sup>

Jeffrey J. Scott<sup>1,3</sup>

1. Audit Committee

2. Compensation & Governance Committee

3. Health, Safety & Environment Committee

### **Auditors**

Ernst & Young LLP

### **Bankers**

National Bank of Canada

Toronto Dominion Bank

Bank of Montreal

Canadian Western Bank

### **Legal Counsel**

Heenan Blaikie LLP

### **Transfer Agent**

Olympia Trust Company

### **Management**

Garnet K. Amundson  
President & Chief Executive Officer

Jeff B. Newman  
Chief Financial Officer & VP, Finance

Kevin W. Job  
VP, Operations

Don A. K. Webster  
VP, Operations

### **Stock Exchange Listing**

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