EDC
EURASIA DRILLING COMPANY LIMITED

Eurasia Drilling Company Limited Annual Report 2010

Eurasia Drilling Company is the largest provider of drilling services in Russia.

We supply onshore integrated well construction services and workover services to national and international oil and gas companies and offshore drilling services in the Russian, Kazakh and Turkmen sectors of the Caspian Sea.

Our objective is to provide the best possible value to our customers and superior returns to our shareholders.

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Highlights

Revenues

+31%

US $1,812 million
(2009: US $1,312 million)

EBITDA

+36%

US $436 million
(2009: US $320 million)

Net income

+25%

US $207 million
(2009: US $165 million)

Earnings per share

1.44

US $ (diluted)

Dividend

0.31

US $ per share

Strategic

- Signed Letter of Intent with Schlumberger to swap assets and to enter a Strategic Alliance in the CIS; transaction completed in April 2011
- Signed drilling contract with TNK-BP, a new client for EDC
- Further diversified our client base, with major customer accounting for 57% of total drilling volumes versus 63% in 2009
- Contracted Lamprell Plc to build a new jack-up drilling rig for our operations in the Caspian Sea
- Fully integrated West Siberian workover assets (purchased December 2009) and added additional capacity in Timan-Pechora through acquisition of Meridian

Operational

- Drilled a record of 4.103 million metres onshore in 2010, 9.3% higher than in 2009
- Maintained position of market leader in Russia's drilling segment with a market share of approximately 24% (based on metres drilled)
- Completed fabrication of our first own-built drilling rig, a 450 tonne cluster-walker named YERMAK
- *ASTRA* jack-up drilling rig fully employed in Turkmen and Russian waters of the Caspian Sea

Financial

- Revenue for 2010 was 31.1% higher than in 2009
- EBITDA increased 36% to US $436 million
- EBITDA margin improved to 24.1%
- Net income increased by 25.3% over 2009

EDC at a glance

EDC in 2010

No.1

We are the largest independent drilling company in Russia, as measured by metres drilled.

18k

Our more than 18,000 highly qualified personnel are committed to satisfying our customers' needs and delivering unmatched service quality.

477

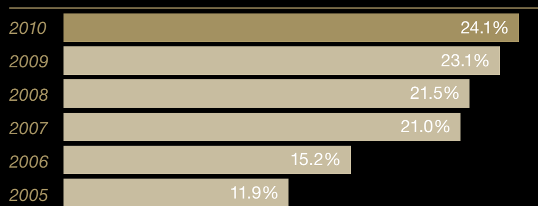
Our rig fleet consists of 211 onshore drilling rigs, 265 onshore workover rigs and the offshore jack-up rig *ASTRA* as of December 31, 2010.

4.1m

We drilled a record 4,103 million metres onshore in 2010.

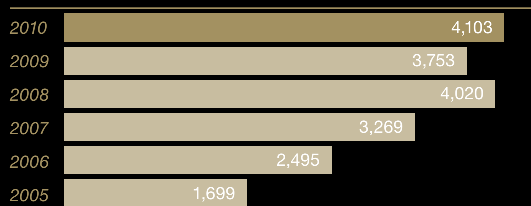
Performance

EBITDA Margin
(%)



Since the Company's inception in 2005 we have doubled our EBITDA margins. Increases in efficiency and modernisation of our rig fleet have been the primary drivers behind our remarkable growth.

Metres drilled
('000s)



From 2005 to 2010 we achieved a 19% compound annual growth rate in meters drilled. This rapid expansion in our output was achieved organically.

Eurasia Drilling Company is now the largest land drilling company in the Eastern Hemisphere. We create value for our clients by utilising the latest drilling technologies and processes.

Market dominance

Being the largest requires us to be the best we can be every day. As our clients' requirements change, so must we.

Onshore

Our onshore drilling services division provides integrated well construction and workover services to Russian and international oil and gas companies, primarily in Russia.

Offshore

Our offshore drilling services division provides drilling and workover of oil and gas wells in the Caspian Sea, serving international E&P companies throughout the region.

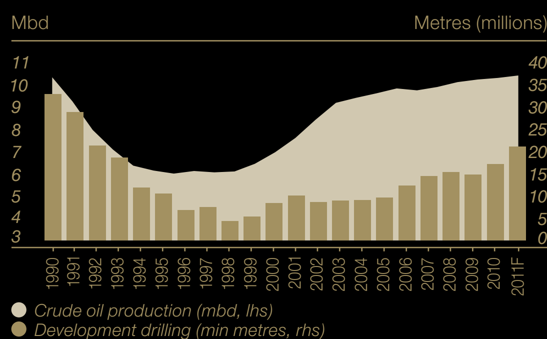
EDC locations

Market overview

Russian oil industry

- Following the dissolution of the Soviet Union crude production and drilling volumes fell sharply.
- From 1999 to 2004 rising oil prices, a revalued ruble and improved economics encouraged capital inflows. Idle well reactivation programs and massive hydro fracturing campaigns boosted oil production significantly, while drilling volumes grew moderately.
- By 2005 idle well inventories had fallen dramatically, and existing-well production intensification techniques were providing diminishing returns. New wells were required to maintain production levels, and drilling volumes have grown significantly in volume terms since then.

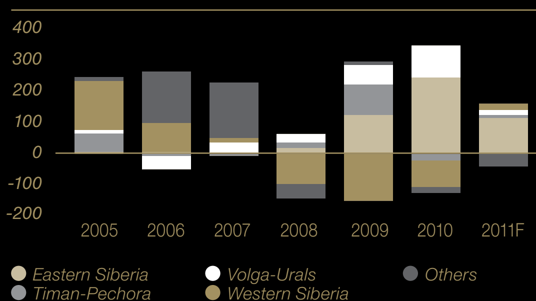
Russian crude oil production and development drilling*



Regional dynamics

- Western Siberian oil production accounts for over 60% of the Russian total but has been declining since 2008 as drilling growth rates have slowed.
- New production from Greenfields in Eastern Siberia, Timan-Pechora, the Caspian and Sakhalin, plus contributions from one-off production enhancements in Volga-Urals, have offset Brownfield declines in recent years, but additional incremental contributions are not expected for the next few years.
- Sustained crude oil output in Russia can only be achieved through mitigation of decline in the Brownfields. These fields lie predominantly in Western Siberia and will require an increased pace of drilling growth from 2010 onwards, in combination with wider application of advanced technologies.

Russian crude oil production change by region*
(kbd)



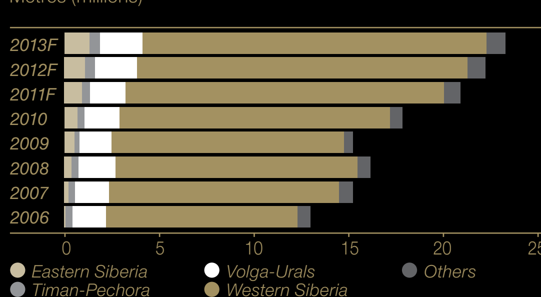
**Russian Upstream and Oilfield Service Industry 2011* by REnergyCo

Russia, with some of the largest hydrocarbon reserves in the world, has an economy that depends on the success of its oil and gas industry. Reserve replacement, maintenance of mature field output and development of remote Greenfield projects will require increasing investments in oilfield services for many years to come.

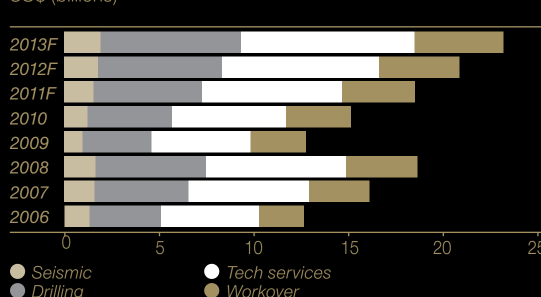
The Russian market is growing rapidly…

- Drilling volumes in Russia grew at more than 8% per year between 2006 and 2010, and are projected to grow at more than 9% in coming years.
- Western Siberia accounted for 80% of the drilling volume in 2010, and it will continue to dominate for many years to come. Greenfield areas are becoming more significant, however, as shown by the predicted 24% annual growth rate in Eastern Siberia.
- In US dollar terms, the market is expected to grow at a faster pace than volume growth would indicate due to the migration of activity toward more remote areas, increases in average well depths and the employment of more complex technologies.
- Sustained growth of over 15% per year is predicted for the overall Oilfield Service (OFS) US dollar market, while the drilling segment is expected to expand at more than 18% per year.

Russian onshore drilling*
Metres (millions)



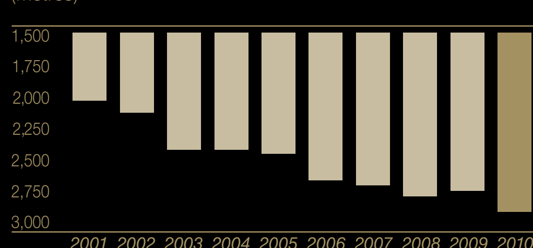
Russian onshore OFS*
US$ (billions)



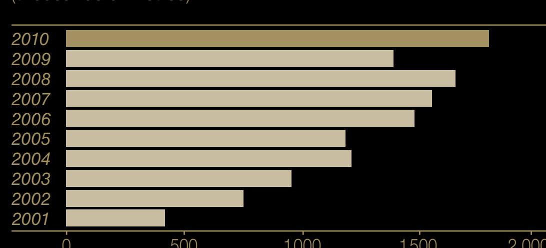
…while drilling is more complex

- A 'typical' well drilled in Russia is 40% deeper today than it was 10 years ago.
- Exploitation of deeper reserves in both Greenfield and mature areas has contributed to the growth in average well depths, challenging the market to deliver higher capacity and more technically advanced drilling rigs.
- Horizontal drilling increases flow rates of production wells, and this technology is becoming increasingly prevalent. Volumes in Russia have more than tripled in the last decade.
- EDC forecasts drilling nearly twice as many horizontal metres in 2011 with our industry leading rig fleet.

Average depth of wells drilled in Russia*
(metres)



Horizontal drilling in Russia*
(thousands of metres)



Acquisition timeline

Throughout our history, EDC's impressive growth has been achieved primarily through organic means. Beginning in late 2009 we embarked on a series of strategic acquisitions which have made us the largest land drilling company in the Eastern Hemisphere.

December 2009
163 workover rigs and associated crews acquired from LUKOIL West Siberia US $21 million

01

December 2009
Acquired OOO Techgeoservice adding Directional Drilling & Telemetry services capability US $35 million

02

June 2010
Workover footprint expanded to Komi Republic (Timan-Pechora region) through acquisition of OOO Meridian US $12 million

03

04

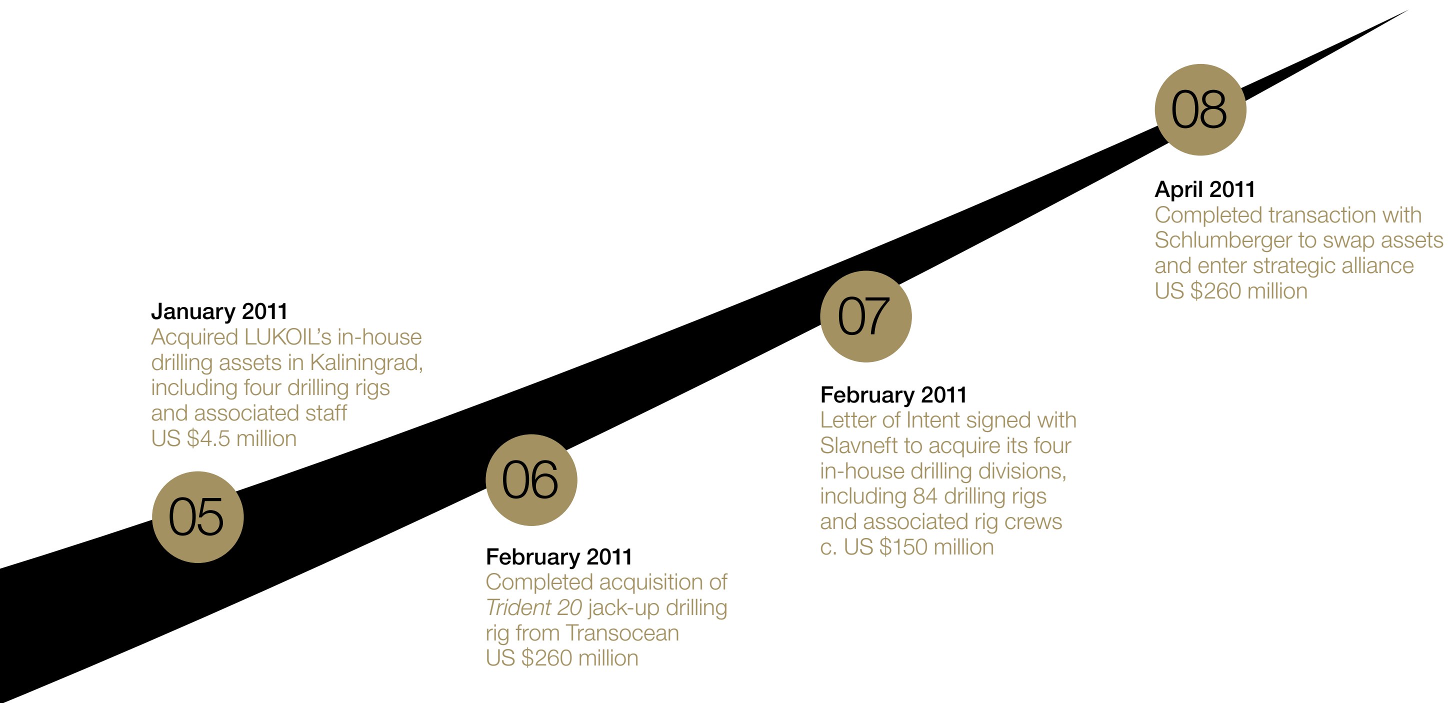
August 2010
Further expanded cementing service offering by acquiring OOO MTU; Slavneft's in-house cementing division US $9 million

Trident 20 jack-up rig acquisition at a glance

- The transaction to acquire the *Trident 20* jack-up from Transocean was announced in January 2011 and closed in February 2011:
  – *Trident 20* is a KFELS CS MOD V independent cantilever jack-up rig
  – The rig is the most advanced jack-up currently deployed in the Caspian Sea, capable of working in water depths up to 350 feet and drilling wells up to 26,000 feet deep
- Acquisition value US $260 million
  – In addition to acquiring the rig, EDC has retained the vast majority of the rig crew and support staff
- The rig has been on continuous contract with Petronas Carigali in Turkmenistan since 2003
- After the completion of the *Trident 20* acquisition EDC controls two thirds of the jack-up rig fleet active in the markets we serve in the Caspian Sea (Russia, Kazakhstan and Turkmenistan).

$675m

Total value of M&A program in 2011 approx. US $675 million



Schlumberger transaction at a glance

- The transaction with Schlumberger was announced late in 2010 and closed in April 2011
- EDC transferred to Schlumberger its cementing assets including OOO MTU & related 24 crews, directional drilling/telemetry assets (OOO Techgeoservice) with 57 crews, drilling fluids assets with 50 crews
- Schlumberger transferred to EDC all of its drilling assets with 19 rigs & 12 crews, workover assets with 34 rigs & 25 crews, and sidetracking assets with 23 rigs & 20 crews
- Strategic Alliance was also formed with Schlumberger as a preferred supplier of drilling services to EDC in the CIS for the next five years
- Total value of transaction approx. US $260 million
- Drilling output of Schlumberger drilling assets in 2010 was c. 700k metres which accounts for c. 4% market share
- 20 Sidetracking crews added to our existing capability gives EDC the largest sidetracking offering in Russia
- Primary clients for the acquired assets are Rosneft & TNK-BP

Chairman's statement

2010 was the year all doubts were extinguished as EDC established itself as the largest land drilling company in the Eastern Hemisphere.

24.1%

EBITDA Margin
An increase in margin of one percentage point compared to 2009

$1,812m

Revenue increased by 31% to US $1,812 million

$207m

Net income increased by 25% to US $207 million

The Earl of Clanwilliam
Chairman

2010 was the year all doubts were extinguished as EDC established itself as the largest land drilling company in the Eastern Hemisphere. On the back of recovering financial markets, strong commodity prices and incipient decline in Russian brown field production, our investors recognised a gain of over 100% as our stock price increased from a little over US $16 at the beginning of the year to US $32.50 at the end of 2010.

Early in the year we promised to deliver on our strategy and drive opportunities. We did both in fine fashion as we delivered outstanding financial results for the year and set the stage for acquisitions and alliances in 2011 which will move EDC into a new sphere of market influence.

Our financial performance for 2010 includes the following highlights:
- Our Revenue increased 31% to US $1.8 billion.
- Our EBITDA increased 36% to US $436 million.
- Our net income increased 25% to US $207 million.
- Our EBITDA margin increased from 23.1% to 24.1%.

Of particular note in 2010 was the amount we paid out in dividends. We paid a one-time special dividend of approximately US $179 million in April (this special dividend was a product of the gain recognised in our 2008–2009 stock buy-back program) and a regular dividend of 31 cents per share in the total amount of $US 45 million which was declared late in 2010 and paid in January of 2011. Few companies in any industry have returned, proportionately, this much cash to shareholders in the recent past.

Through the end of 2010 our growth has been primarily organic. We tripled our drilling metre output, doubled our EBITDA margins and radically increased our drilling efficiency from early 2005 when we began work as an independent oil and gas drilling company. Towards the end of 2010 we began the next phase of our growth as we announced the acquisition of all of Schlumberger's drilling, workover and sidetracking assets in the CIS and also announced the acquisition of the drilling assets of Slavneft. Both of these transactions will be completed in 2011, along with a third important acquisition—that of the *Trident 20* jack-up drilling rig, which is currently under a long-term contract to Petronas in the Turkmen waters of the Caspian Sea. In addition we began work on a new, high-spec, jack-up drilling rig which will be completed in late 2012 and will go to work in the Caspian Sea in early 2013. The result of these recent moves is that we will have an onshore market share in Russia of approximately 32% and an offshore market share in the Caspian Sea of approximately 66% in 2012. Both of these markets are slated to grow at very high rates for the foreseeable future. We expect to grow with them.

The next few years should be good ones for our shareholders, clients and employees. We still see many opportunities for both organic and inorganic growth and also see specific areas in which we can continue to improve our operations and resulting financial performance. The drilling rig fleet is aging in Russia while the demand for heavier and more capable rigs continues to increase. Well capitalised companies like EDC are best positioned to perform in such environments.

I would be remiss if I did not say something about safety and environmental compliance. During 2010 the industry, worldwide, did much soul searching after the Macondo incident in the U.S. Gulf of Mexico in April. The message was clear—the price of safety is eternal vigilance. In May, in concert with the regulatory authorities in the Caspian Sea, we participated in an oil spill drill to test our systems and response measures. Our people performed well and in accordance with expected norms. While the oil drilling business is inherently a dangerous profession we do our best to minimise injuries. For the year our Total Reported Incident Rate decreased to a level below that of the rest of the industry and, I am very pleased to report, we had no job related fatalities among our 18,000 employees.

I wish to express my appreciation and thanks to the other members of the Board for their attention and dedication to our business during 2010, to the management team for their outstanding performance during 2010 and to our clients and shareholders for their continued patronage. It is my single pleasure to be associated with EDC.

The Earl of Clanwilliam
Chairman
21 June 2011

For more information about our year visit
www.eurasiadrilling.com

Chief Executive's strategic review

In 2010 the Company proved it could deliver. We drilled a record number of metres while producing enviable financial results.

Alexander Yu. Djaparidze
Chief Executive Officer

In 2010 the Company proved it could deliver. We drilled a record number of metres while producing enviable financial results. We expanded our client base, reducing our reliance on one customer. We expanded our product offering – increasing our workover operations. At the same time we proved we could make strategic moves to set the stage for future growth. We negotiated acquisitions and strengthened our management team in both the onshore and offshore arenas – giving us the most stable and geographically diverse footprint for growth in Russia.

But it is not only about growth and market share. It is also about providing a high level of service to clients and being responsive to their changing needs. Drilling in Russia is becoming more complex and the wells are becoming progressively (and precipitously) deeper. This requires new technologies and heavier equipment. Accordingly, we have recently ordered twenty-four new heavy drilling rigs to be delivered over the next two years and have formed an alliance with Schlumberger, the largest and arguably most technically advanced oil field services company in the world, to ensure we will be able to provide the quality and volume of services required by our clients into the future.

In 2010 we did the following:

- Increased our metres drilled by 9% to 4.1 million metres
- Diversified our client base with our largest client decreasing to 57% of our volume
- Integrated our new workover operations into our larger organisation
- Responded to changing client needs by drilling some of the first underbalanced wells in Russia
- Acquired an important new drilling client – TNK-BP
- Ordered a new high-specification jack-up drilling rig for the Caspian Sea
- Negotiated financially attractive agreements with Slavneft and Schlumberger to further expand our size, product offerings and client base

When we did our initial public offering in late 2007 we set forth a five-part strategy. I am proud and pleased to say we are well on the way to achieving what we said we would do.

We said we would increase our market share in Russia. At the time of the IPO our market share was a little over 20%. By the end of 2011 our market share will be closer to 32%. We said we would increase our customer base. By the end of 2011 our largest customer will account for well under 50% of our metres drilled, down from 77% at the time of our IPO. We said we would expand our offshore drilling. By the middle of 2013 we will own three of five jack-up drilling rigs in the Caspian Sea; two of which will have world-class drilling capabilities. In addition we are the general contractor for the largest platform drilling operation in the Russian sector of the Caspian Sea. We said we would expand and improve our workover capacity. With the addition of the Schlumberger workover assets acquired in April 2011 we will have the largest workover and largest sidetracking fleets in Russia, in addition to the largest drilling fleet. We said we would broaden our technology base. We recently formed the previously mentioned alliance with Schlumberger which will allow us to jointly bid for work to provide the most up-to-date package of services to our clients anywhere in the CIS.

While we are proud of what we have accomplished we do not intend to rest on our laurels. During 2010 we completed a pilot program to drill under balanced wells for one of our clients. The results from this pilot program have reportedly been very good and our client has asked us to extend and expand the program for 2011. Also during the first quarter of 2011 our horizontal drilling doubled from the same period in 2010. These kinds of wells require heavier rigs with larger mud pumps and also require a greater component of third-party services requiring us to successfully manage a more complicated logistics flow. In short, our business is changing and so we must change with it. We expect that our clients will further experiment with newer technologies to deal with lower reservoir pressures in older brown fields and the greater percentage of fractured and discontinuous reservoirs in some of the green field areas. We are confident we can respond to these market changes with offerings that are fairly priced and competently managed.

In addition the day-to-day management of our Company never stops. We continue to see incremental areas where we can make improvements in our processes and cost structure to further enhance our margins.

As the fourth largest drilling company in the world, measured by market capitalisation, we are privy to possibly interesting acquisitions both within Russia and further afield in the Eastern Hemisphere. We are looking at some of these opportunities where we think we can add value. Our policy has been to look before we leap. We will not grow simply for growths' sake but rather seek situations that have a high probability of being value accretive.

Our success, both past and future, relies on many things – the guidance from our Board of Directors and the executive abilities of our management team — but most of all it relies on the dedication of our 18,000 employees who are ultimately responsible for product delivery. We strive to make EDC a rewarding place to work where employees can have meaningful careers, benefiting their families and communities.

Alexander Yu. Djaparidze
Chief Executive Officer
21 June 2011

Key strategic focus

01	Increase market share	• Acquire up to two in-house and/or independent drilling companies • Continue to invest in fleet expansion and upgrades • Leverage capacity and efficiency leadership to gain market share with existing customers
02	Growth of customer base	• Target acquisition of businesses with diverse customer portfolios • Continue to differentiate ourselves from our competitors in our domestic markets • Evaluate other strategic opportunities outside of Russia and the CIS
03	Expansion in offshore drilling	• Commission new offshore drilling assets in response to market developments • Consolidate the market through acquisition of existing assets where possible • Develop offshore extended-reach drilling capability
04	Expand & improve workover capacity	• Conclude integration of W. Siberia W/O assets acquired in 2009 within existing workover structure • Target selected acquisitions of additional workover and sidetracking capacity
05	Broaden technology platform	• Expand and improve core drilling service offerings in advance of divestiture • Develop and promote strategic partnerships with global technology leaders • Invest in state-of-the-art drilling rigs and systems to meet our clients' requirements for more complex and technically challenging wells

Management's discussion and analysis of financial condition and results of operations

We continue to adopt new drilling technologies in order to be in a position to satisfy our customers' demands for more technologically advanced and complex services.

Introduction

The following report represents management's discussion and analysis of financial condition and results of operations for the 12 month period ended December 31, 2010 and is intended to help our shareholders and other users of our financial statements better understand our operations and attendant financial results and current financial condition. This information is provided as a supplement to, and should be read in conjunction with our audited 2010 Consolidated Financial Statements and the accompanying notes, prepared in accordance with US GAAP. This discussion should not be considered all inclusive as it does not necessarily include all changes regarding general economic, political, governmental and environmental events. As used in this report, 'Company', 'we,' 'us,' 'our' and 'EDC' means Eurasia Drilling Company Limited and, where the context requires, includes our subsidiaries.

This report contains forward-looking statements that involve known and unknown risks, uncertainties and other factors which may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements.

Nature of operations

Eurasia Drilling Company Limited is one of the leading onshore & offshore providers of oil & gas development and exploration well drilling services in the CIS. We offer onshore integrated well construction and workover services to local and international oil and gas companies primarily in Russia, and offshore drilling services to Russian and international oil and gas companies in the Russian, Kazakh and Turkmen sectors of the Caspian Sea.

Our customers include a number of the major Russian and international oil and gas companies such as LUKOIL, Rosneft, Gazpromneft, TNK-BP, KazMunaiGaz affiliates, Samara-Nafta, Naryanmarneftegaz (a joint venture between LUKOIL and ConocoPhillips), CMOC (a joint venture between Shell, KazMunayTeniz and the Oman Pearls Company Ltd), Dragon Oil and others. Petronas Carigali became a new client to us starting early 2011 post the purchase of the *Trident 20* jack-up drilling rig from Transocean.

01

Strategic focus 01

Increase market share

- EDC acquired drilling assets from Schlumberger in April 2011 which will add 3–4% to our drilling market share on a full year basis
- In 2011 we intend to complete the acquisition of in-house drilling assets from Slavneft which will add a further 3–4% to our drilling market share (full year basis)
- In 2010 we implemented our 5-year fleet replacement and expansion program, ordering 24 high-capacity drilling rigs for 2011/2012 delivery as a first stage
- By 2012, roughly one in three new wells in Russia will be being drilled by EDC rigs and crews

Our operational objective is to deliver value added services to our clients while continuously improving the quality of our asset base. We have established a strong presence in each of the major oil producing regions within our served market. As of 31 December 2010 our total land rig fleet of 476 rigs included 211 land drilling rigs and 265 workover rigs, and we employed over eighteen thousand personnel. We continue to adopt new drilling technologies in order to be in a position to satisfy our customers' demands for more technologically advanced and complex services.

We entered the onshore drilling and workover services business in December 2004 by acquiring substantially all of the onshore drilling and certain related assets of OAO LUKOIL. Since inception we have not substantially relied on acquisitions to increase our share of the onshore drilling market. We were able to transform the Company from an in-house cost centre to an independent oilfield service provider with sound finances and materially improved operational efficiency. We recently began the next phase of our development by signing a Letter of Intent with Schlumberger to sell and purchase each other's drilling and service assets and to enter into a Strategic Alliance in the CIS. Further, in early 2011 we signed a Letter of Intent to purchase the in-house development and exploration drilling assets of Slavneft.

In December 2006, we entered the offshore drilling business by acquiring the offshore drilling business of OAO LUKOIL, which primarily consisted of the ASTRA, a floating jack-up drilling rig located in the Caspian Sea. We continue to build momentum in the Caspian Sea. In November 2010 we contracted Lamprell to build a new hi-spec jack-up rig, the completion of which is expected late in 2012. Early in 2011 we expanded our current offshore rig fleet to two jack-up rigs by acquiring *Trident 20* from Transocean. As such, in 2011 we have the capacity to serve approximately two-thirds the jack-up market in the Russian, Kazakh and Turkmen waters of the Caspian Sea. We continue to provide platform drilling services in the Northern Caspian Sea to LUKOIL for its Yuri Korchagin development, which we commenced near the end of 2009.

In 2011 we will concentrate on project execution, and expect to deliver strong financial and operating results.

Overview

Demand for drilling services depends on a variety of factors, including worldwide demand for oil and gas, the ability of OPEC to set and maintain production levels and pricing, the level of production of non-OPEC countries and the policies of the various governments regarding exploration and development of their oil and gas reserves. Our results of operations depend on the levels of activity in Russia and countries of the Caspian Sea, and the prices of crude oil and natural gas in Russia. To date most of our drilling activities have been in oil provinces rather than gas provinces. This business mix may slowly change over time if we obtain new clients whose activities are more heavily weighted to drilling natural gas wells.

The oilfield services market in Russia is robust, and it is arguably the most stable land market of any size in the world. Onshore drilling activity (as measured by wells or metres drilled) fell in 2009 as compared to 2008 by only around 6%, which was substantially less than the reductions in drilling activity experienced in the world's other large markets. Following the global recession the oil prices stabilised in 2010 in the range of US $70 to US $80/bbl giving oil and gas companies confidence to increase their CAPEX budgets. Russia's oil production and drilling volumes both reached post-Soviet peaks in 2010; oil production grew to 10.14 mln bpd (an increase of 2.2%) and drilling volumes expanded to 17.2 million metres (an increase of 18%), respectively, as compared to 2009 according to CDU TEK.

The major contributor to the Russian oil production growth was the increased output from certain Eastern Siberian fields. Growth in drilling volumes was mainly achieved through increased drilling in mature fields which account for about 80% of Russia's total oil production.

During 2010 our business continued to benefit from favourable market conditions resulting primarily from fairly stable commodity prices and a resulting increase in demand for our services. This increased demand was met by adding drilling crews, adding new rigs to our fleet and improving utilisation of our rig fleet.

Our 2010 operating results include:

- drilling output of 4.103 million metres, a record drilling volume during our operating history, 9% above the output achieved in the corresponding period of 2009 (3.753 million metres);
- at the beginning of October 2010 we signed a Letter of Intent with Schlumberger to sell and purchase each other's drilling and service assets and enter into a Strategic Alliance in the CIS;
- contracted Lamprell Plc to build a new jack-up drilling rig to be used in our Caspian Sea operations;
- further diversified our customer portfolio by commencing drilling operations for TNK-BP, a new client for EDC, in May 2010;
- reduced our reliance on our largest customer in 2010 with its' share comprising 57% of our total drilling volumes compared to 63% in the corresponding period of 2009;
- fully employed our jack-up rig, ASTRA, in Turkmen and Russian waters of the Caspian Sea; two production wells and three exploration wells were drilled and completed;
- continued operations on LUKOIL's Yu. Korchagin field platform in the Caspian Sea, drilling four wells;
- remained active with two drilling rigs in Kazakhstan; seven wells were drilled and completed;
- completed fabrication of our first 450 ton drilling rig named 'YERMAK' in March 2010.

24%

Our market share for 2010 was 24% of total metres drilled onshore Russia

Management's discussion and analysis of financial condition and results of operations continued

Our main clients are the four largest E&P companies in Russia, which together accounted for well over half of all new wells drilled in 2010.

Major Events post December 31, 2010

- In February 2011 we signed a Letter of Intent to purchase the development and exploration drilling assets of OAO NGK Slavneft for a total consideration of US $150 million. We expect to close the transaction later in 2011. In addition, Slavneft and EDC have agreed to develop a Framework Agreement for the provision of drilling services by EDC to Slavneft following the acquisition. The Framework Agreement will cover a five year term commencing at the completion of the transaction and will include pricing terms, annual price adjustment provisions and commitments for drilling volumes. This new partnership with Slavneft is another important step in expanding our client base;
- In February 2011 we completed the acquisition of the *Trident 20* jack-up drilling rig from Transocean for a total consideration of US $260 million. The *Trident 20* is a Keppel FELS CS Mod V cantilever jack-up capable of operating in water depths to 350 feet and capable of drilling to 26,000 feet. The rig is presently operating in the Turkmen waters of the Caspian Sea on a long-term contract with Petronas Carigali (Turkmenistan) Sdn Bhd, which runs through 2012. The acquisition of the *Trident 20* is a milestone on our path to become the market leader in the Caspian offshore drilling market.

57%

Our largest customer accounted for 57% of our metres drilled in 2010, down from 63% in 2009

Our Russian onshore drilling volumes increased 9% compared to volumes achieved in 2009. The drilling volumes of our major customer declined by 1% during the 2010 as compared to the corresponding period of 2009. LUKOIL's share in our total volumes decreased to 57% in 2010 from 63% in 2009. It's our strategic goal to diversify our customer base while building long-term relationships with our clients. TNK-BP, a new client to us, contributed 2% of our 9% growth in metres in 2010. As of the end of 2010 we had four drilling rigs operating for TNK-BP. Though the share of TNK-BP in our total drilling volume is not yet significant, we are determined to increase the scope of work for TNK-BP by providing best-in class equipment and a high standard of performance. We gained additional volumes with other clients during 2010 including Gazpromneft, which accounted for 29% of our total drilling volumes as compared to 24% during 2009. The list of our clients includes the four largest E&P companies in Russia which, together, accounted for about 56% of the total drilling volumes in Russia in 2010 based on CDU TEK data. In 2010 we also won important contracts with another four new clients, including Pechoraneft and Rusvietpetro.

Our market share for 2010 was approximately 24% which is slightly below the corresponding period of 2009. The reduction was primarily caused by an increase in drilling by the in-house drilling divisions of some Russian oil and gas majors, especially Surgutneftegas, whose drilling volumes increased 15% and reached 4,430 thousand metres in 2010 as per CDU TEK.

The drilling pattern in 2010 was characterised by greater seasonality than in 2009, but very similar to 2008. There was a slow start at the beginning of the year caused by severe winter conditions in West Siberia as well as higher exploration activity (which occurs during the ice-road season and ties up rigs by isolating them in remote areas). As per CDU TEK data, exploration drilling volumes in onshore Russia during 2010 were above the corresponding period of 2009 by 53%. Starting in March drilling accelerated reaching its peak in May 2010. In May 2010 we drilled 398 thousand metres – a record for our operating history.

During 2010 we expanded our drilling rig fleet to a total of 211 drilling rigs as compared to 207 at the end of 2009. Late in 2010 we added two new rigs for our new client, TNK-BP. Management believes that the effective age of our rig fleet is much less than Russia's average of 18–19 years as per Douglas Westwood data. The services market in Russia is evolving toward higher technological content and advanced techniques. In Russia, as in the rest of the world, unexploited oil and gas reserves increasingly occur in more challenging environments, both geographically and geologically. As technology applications advance, so do the costs of bringing a barrel of hydrocarbons to market. To justify the higher costs, technologies must deliver greater efficiencies and production potential to the oil and gas producers. To satisfy this requirement and to ensure the stability and further growth of oil production in Russia, we expect a strong requirement for new modern rigs. To meet this requirement the Company has developed a five year rig fleet upgrade and modernisation plan according to which 18 rigs were ordered in 2010 with the delivery times during 2011. US $61.7 million was allocated as of December 31, 2010 to pay for the first five rigs. The drilling rigs that we are ordering are produced by Russian and Chinese manufacturers at prices significantly lower than in 2008 and with shorter lead times.

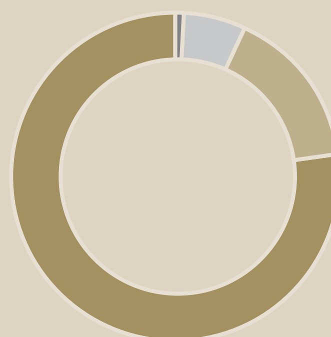
02

Strategic focus 02

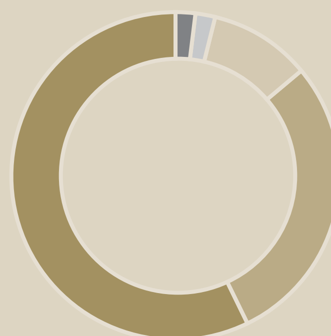
Growth of customer base

- TNK-BP, Russia's 3rd largest oil producer, became our customer in 2010 and our share of their business is growing in 2011
- Schlumberger and Slavneft transactions will contribute markedly to our customer diversification: SLB assets work primarily for Rosneft & TNK-BP, Slavneft assets for Slavneft
- In 2011 our major client, LUKOIL, will account for 50% or less of our total metres drilled, as compared to 77% in 2007 (EDC's IPO year)

Client Mix Mid-Year 2007 [at time of IPO]
(% of metres drilled)



Client Mix 2010
(% of metres drilled)



In March 2010 we completed the fabrication of a 450 metric ton high-spec rig named 'YERMAK'. This rig design is unique within Russia, featuring a 'Quadra' moving system which enables it to walk and turn in any direction. Another unique feature is a separate, fixed mud block incorporating mud pumps, tanks and processing equipment coupled with a flexible interconnecting umbilical system that conducts drilling fluids, steam and electrical energy and control systems cabling. This is the first rig incorporating such features to be designed for operations in Russia's specific environment, characterised by extremely cold winter conditions, warm summer temperatures and limited transport networks. The rig is designed for deep cluster drilling applications since approximately 95% of the production wells in Russia are drilled directionally from pad clusters, while wellbore lengths are trending toward longer reach and deeper reserve targets.

In June 2010 we acquired a Russian workover service company in the Komi Republic, Timan-Pechora region. In the beginning of August 2010 we acquired a Russian provider of cementing services with operations mainly located in West Siberia. The value of two acquisitions in total was approximately US $20 million.

Our offshore operations remained strong during 2010. Our jack-up rig, ASTRA, was fully booked and employed in the Turkmen and Russian waters of the Caspian Sea during 2010. Five wells were drilled and completed. In June 2010, *ASTRA* participated in an international exercise aimed at the offshore emergency response operations for possible oil spills in the Northern part of the Caspian Sea. *ASTRA* was used as a control centre and successfully performed as expected during the exercise.

We have contracted Lamprell Plc to build a new jack-up drilling rig to be used in our Caspian Sea operations. The new jack-up rig is a LeTourneau designed Super 116E self-elevating Mobile Offshore Drilling Platform, designed to operate in water depths of up to 250 feet (extendable to 350 feet as required) and will have a rated drilling depth of 30,000 feet. The hull and related components are to be pre-fabricated by Lamprell in its Sharjah facility, while the remaining component fabrication, final assembly and commissioning will be performed at a shipyard in the Caspian Sea. Construction is expected to be completed at the end of 2012. The demand for jack-up rigs in the Caspian Sea has reached a level where we are confident that this new high-spec rig will be fully contracted for several years at favourable operating rates, when it is commissioned.

We continue our operations on LUKOIL's Yuri Korchagin field platform and drilled four wells during the 2010 including one vertical and three directional wells.

Management's discussion and analysis of financial condition and results of operations continued

26,000ft

The *Trident 20* is rated to drill wells up to 26,000 feet deep

Transaction with Schlumberger

In October 2010 we signed a Letter of Intent with Schlumberger, the world's leading oilfield services company, to exchange assets and to enter into a Strategic Alliance in the CIS. Schlumberger has agreed to sell all drilling (19 drilling rigs), sidetrack (23 sidetracking rigs) and workover rigs (34 workover rigs) currently operating mainly in West Siberia to EDC. As part of the sale, the rigs' crews (12 drilling crews, 20 sidetracking crews and 25 workover crews) will transfer to EDC. Schlumberger has also agreed to purchase the Company's drilling services businesses, which include the directional drilling, measurement while drilling, cementing and drilling fluids services to support 80 rigs. The field crews to support delivery of these services will move to Schlumberger. In addition, Schlumberger and EDC have agreed to enter into a Strategic Alliance upon completion of the transaction whereby Schlumberger becomes the preferred supplier of drilling services to Eurasia Drilling Company for a 5-year period.

We see this transaction as a foundation of a long-term relationship between two industry leaders. Importantly, we will have guaranteed access to the latest technologies from Schlumberger to offer more complex onshore and offshore drilling solutions. The businesses that we are acquiring from Schlumberger are well managed and have established sound reputations as efficient and reliable service providers. Rosneft and TNK-BP are the largest customers for drilling and workovers, respectively. The rigs that we are adding are in the appropriate condition and supportive to the average age of our rig fleet, which post completion of the transaction will be one of the most modern in Russia.

Outlook

Global oil prices were resilient throughout 2010, averaging over US $80/barrel for Urals 32° crude in the second half of the year. Oil prices have continued to gather strength this year, averaging over US $100/barrel in the first quarter of 2011. NYMEX futures prices for crude oil currently show that prices are expected to remain above $100/barrel (WTI) for the rest of the decade.

In the Russian market, most commentators forecast the rapid growth of new well starts in 2010 versus the previous year to continue into 2011 and beyond. Indeed, during the first few months of 2011, growth in drilling volumes in Russia has outpaced the 2010 growth rate year-on-year, according to CDU TEK.

03

Strategic focus 03

Expansion in offshore drilling

- In November 2010 we contracted Lamprell to build a new LeTourneau Super 116E jack-up rig for the Caspian, due for commissioning in early 2013
- In February 2011 EDC acquired the *Trident 20* jack-up rig from Transocean, and we retained the majority of the rig crew. The KFELS CS MOD V rig is on long-term contract with Petronas in Turkmenistan
- During 2011 the drilling package on LUKOIL's Yuri Korchagin platform, where EDC is employed as the general contractor for drilling, will be upgraded for extended-reach drilling and our crews will be trained in advanced ERD techniques

Relatively milder weather conditions in West Siberia coupled with robust commodity prices have contributed to the increasing growth rate early in the year, while the longer term outlook for sustained drilling demand growth in Russia remains underpinned by declining brownfield production.

Strategies to enhance upstream efficiency, including increases in new-well flow rates and improvements to the recovery factor on existing reserves, are progressively being pursued by our customers. A strong indicator of this trend is the increase in the number of horizontal production wells being planned, which we expect to rise substantially within our client base beginning in 2011. As an example, our largest customer, LUKOIL, has stated its intention to treble the number of new horizontal wells drilled in coming years. Meanwhile, we perceive a tightening in the supply of suitable drilling rigs, particularly in the higher specification and heavier rig classes. Pricing for drilling services has not yet been significantly impacted by supply constraints, but we believe pricing power may begin to favour contractors as indicated by certain of our clients' expressed interest in establishing multi-year contracts.

For 2011 we expect our onshore drilling volumes to exceed 2010 volumes by over 15%, reaching the level of approximately 4.8 million metres drilled. This estimate includes both improvements in legacy output and prorated contributions from acquisitions. Actual closing dates of the Schlumberger and Slavneft acquisitions, which we anticipate to be early Q-2 and late Q-3 2011, respectively, will affect total volumes achieved this year. EDC's market share in drilling volume terms is expected to increase from 24% achieved in 2010, to the level of 30–32% by Q-4 2011 on an annualised basis.

The Company's revenue growth is anticipated to outstrip volume growth in 2011 as our customers increasingly drill more horizontal wells, extend lateral reach and expand complexity. As noted earlier, the average depth of wells drilled by EDC has been increasing markedly in recent years. We expect this increasing depth trend to continue, and to drive the market toward higher specification and heavier drilling rigs as well as more complex supporting technologies.

The Company's client mix is projected to diversify further in 2011, with gains in drilling volumes for both TNK-BP and Rosneft and the addition of Slavneft as a customer later in the year. LUKOIL volumes are also expected to increase slightly in 2011 v. 2010, but due to gains with other clients, LUKOIL drilling is projected to account for less than 50% of EDC's total drilling volume (in 2010 LUKOIL accounted for 57% of total EDC drilling volume).

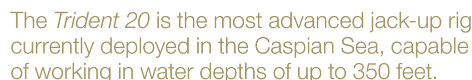
The well intervention market in Russia is projected to expand in 2011 as high oil prices encourage efforts to prolong and enhance existing well production. Workover and sidetracking activity are expected to be strong contributors to the Company's revenue in 2011 as we fully integrate the workover assets acquired from LUKOIL in early 2010, and through the subsequent addition of the workover and sidetrack fleets being acquired from Schlumberger. In addition to our comprehensive well servicing and workover workscope for LUKOIL West Siberia, the Company has been awarded a new workover contract for Rosneft in Vankor, East Siberia, which commences Q-2 2011. The additional workover assets being acquired from Schlumberger (34 rigs, 25 crews) are well utilised and primarily contracted to TNK-BP in their Samatlor field, representing a new area of activity for EDC. The new sidetrack capacity (23 rigs and 20 crews) being acquired by EDC from Schlumberger is also well utilised, with a broad contracted workscope for a variety of customers in 2011.

By the end of 2011, following consolidation of the Schlumberger and Slavneft assets into our operations, EDC will be not only the largest well construction contractor, but also the largest provider of workover, well servicing and sidetracking services in Russia.

EDC has established a significant offshore presence, beginning our first platform drilling services contract in 2009 and adding a second jack-up rig (the *Trident 20*) to our fleet in early 2011. The *ASTRA* jack-up drilling rig is committed for a full 12 month program in 2011 in the Russian and Kazakh sectors of the Caspian Sea, and is currently deployed in Kazakh waters at an attractive day-rate. The *Trident 20* is expected to be fully utilised for development drilling in Turkmen waters in 2011, under long term contract to Petronas Carigali. On-going operations on LUKOIL's Yuri Korchagin field ice-resistant platform, where EDC is the General Contractor for drilling services, are expected to continue for most of the year prior to a drilling package upgrade in preparation for the Extended Reach Development (ERD) phase. The Company will further expand our Caspian fleet when the Super 116E jack-up being constructed by Lamprell enters service in 2013, and we continue to evaluate opportunities for further expansion in this growing market.

Recent appreciation in the Russian ruble with respect to the US dollar is expected to improve our reported results for 2011 over 2010 as most commentators are confident the ruble will stay relatively strong.

During the first half of 2011 we will be integrating two high-quality acquisitions into our operations which will provide, in both instances, accretive financial results in the short term while acting as strong platforms for future growth. Later in the year the Company expects to commence incorporation of the Slavneft drilling assets into our business, expanding both our client base and our geographic footprint. We continue to evaluate other opportunities both within and outside Russia and the CIS. Meanwhile, our historical businesses continue to perform well and grow with their markets. We expect 2011 to be an outstanding year for all our stakeholders.



The *Trident 20* is the most advanced jack-up rig currently deployed in the Caspian Sea, capable of working in water depths of up to 350 feet.

Management's discussion and analysis of financial condition and results of operations continued

Financial Review

During 2010 we achieved remarkable financial results across all lines and geographies of our business that exceeded our initial expectations. We continued to concentrate on execution backed by our ongoing investment in drilling rig fleet modernisation and upgrade. Our 2010 results reflect the revival in the overall drilling market activity as compared to 2009.

Our 2010 financial results include:

- Revenue for 2010 was US $1,812 million, which is US $430 million above US $1,382 million reported for FY 2009;
- EBITDA margin improved to 24.1% for 2010, which is one percentage point above 23.1% EBITDA margin for 2009;
- 2010 Net Income was US $207 million which is US $42 million above Net Income reported in 2009 (US $165 million);
- Diluted earnings per share for the fiscal year ended December 31, 2010 were US $1.44 (2009 diluted earnings per share were US $1.22);
- 2010 average US dollar exchange rate was 30.4 rubles per US dollar as compared to 31.7 rubles per US dollar in 2009, a percentage change of 4.1%.

Reconciliation of Net Income to EBITDA

Earnings before Interest, Taxes, Depreciation and Amortisation (EBITDA), a non-GAAP financial measure, is computed with reference to the Company's net income for 2010 and 2009 as follows (in thousands of US dollars, audited):

	2010	2009
Net income	**207,353**	165,490
Income tax expense	**71,812**	43,857
Gain on disposal of PP&E	**(6,344)**	(382)
Currency transaction loss	**7,355**	4,414
Net gain on acquisitions of businesses	**(557)**	(2,849)
Goodwill impairment loss	**7,096**	–
Interest income	**(7,993)**	(10,631)
Interest expense	**15,125**	13,524
Depreciation	**142,000**	106,390
EBITDA	**435,847**	319,813

Revenues

The following table sets forth a summary of our operating results for 2010 and 2009 (for additional information, please see the accompanying audited 2010 Consolidated Financial Statements).

Consolidated statements of income for the fiscal years ended December 31, 2010 and December 31, 2009 (All figures in thousands of US dollars, unless otherwise noted, audited):

Components of net periodic benefit cost were as follows:

	2010	2009
Revenues		
Drilling and related services	**1,798,881**	1,362,222
Other sales and services	**13,275**	19,981
Total revenues	**1,812,156**	1,382,203
Cost of services	**(1,195,891)**	(912,050)
Selling, general and administrative expenses	**(106,920)**	(94,861)
Taxes other than income taxes	**(72,547)**	(55,061)
Depreciation	**(142,000)**	(106,390)
Gain on disposal of property, plant and equipment	**6,344**	382
Goodwill impairment loss	**(7,096)**	–
Income from operating activities	**294,046**	214,223
Interest expense	**(15,125)**	(13,524)
Interest income	**7,993**	10,631
Currency transaction (loss)	**(7,355)**	(4,414)
Net gain on acquisitions of businesses	**557**	2,849
Other expenses	**(951)**	(418)
Income before income taxes	**279,165**	209,347
Income tax expense	**(71,812)**	(43,857)
Net income	**207,353**	165,490
Basic earnings per share of common stock (US dollars)	**1.45**	1.22
Diluted earnings per share of common stock (US dollars)	**1.44**	1.22

Our total dollar-expressed revenues increased by US $430.0 million, or 31.1%, to US $1,812.2 million for 2010 from US $1,382.2 million in 2009.

The financial results of operations in US dollars for 2010 were influenced by several factors including an increase in our number of metres drilled, an integration of the new workover businesses and changes in the mix of services as well as ruble appreciation. Revenue from offshore operations also contributed to total revenue growth during the fiscal year ended December 31, 2010.

Cost of services

Cost of services includes the following (in thousands of US dollars, audited):

	2010	2009
Services of subcontractors	**488,950**	320,379
Materials	**218,916**	218,718
Wages and salaries	**324,924**	222,603
Fuel and energy	**79,530**	63,581
Transportation of employees to drilling fields	**23,358**	28,143
Leasing and rent	**10,891**	10,857
Other	**49,322**	47,769
Total cost of services	**1,195,891**	912,050

Cost of services increased by US $283.8 million, or 31.1%, to US $1,195.9 million for 2010 from US $912.1 million for 2009. Cost of services as a percentage of total revenue did not change from 2009 to 2010 staying at 66.0%. We believe that this stabilised margin, despite changes in the mix of services (drilling deeper wells and higher levels of horizontal drilling), was primarily attributable to sustained cost control efforts by management.

We generally subcontract with third parties to provide us with certain services in our onshore division in instances where we do not perform these services ourselves. In our onshore division, services contracted from third parties include subcontracting for technological services; transportation services; preparatory services; well facility services; petrophysical services; well services; drilling motor and drilling navigation services; cementing services; and drilling bit services. Services of subcontractors were the largest component of our cost of services during both 2010 and 2009. For the fiscal year 2010, services of subcontractors were US $489.0 million, or 40.9% of total cost of services, as compared to US $320.4 million, or 35.1% of total cost of services for 2009. The increase in total dollars expended was primarily a function of the growth in the volume of workover services provided by the group during 2010 due to the acquisition of workover business late in 2009, an increase in pass-through development services (along with corresponding revenue increase) and change in the mix of services (drilling deeper wells and higher levels of horizontal drilling). The change as a percentage of total cost of services is primarily caused by an increase in transportation costs in the Perm and Komi regions due to the sale of our own non-core transportation assets to a third parties and an increase in the number of turnkey well requests from our customers along with changes in the mix of services.

Expenditures for materials have been primarily influenced by our customers' particular drilling programs and projects. Materials for our onshore and offshore drilling divisions primarily include spare parts, tubular goods, chemicals and cement and drilling tools. Materials costs for 2010 were US $218.9 million, or 18.3% of total cost of services as compared to US $218.7 million, or 24.0% of total cost of services for 2009. The decrease in the percentage of total costs is mostly caused by a change to a different scheme of casing pipe financing instituted by some of our major customers late in the first quarter of 2009. Prior to the first quarter of 2009 casing pipe was included in the price of well construction and in cost of sales. In 2009 certain of our major customers chose to finance a portion of their casing pipe and provide it to us. In 2010, even more of our major customers decided to operate under the new casing pipe financing scheme leading to the continued decrease of material costs as a percentage of total cost of services.

Employee wages and salaries include costs of our personnel directly engaged in providing onshore and offshore drilling and other services. Employee costs include amounts we pay in support of our private employee insurance and medical funds. Such expenses do not include contributions which we make to a private pension fund or social taxes we pay to the Russian government. Wages and salaries for the fiscal year 2010 were US $324.9 million, or 27.2% of total cost of services as compared to US $222.6 million, or 24.4% of total cost of services for 2009. The increase in both total dollars expenses and the percentage of total cost of services was caused by the integration of the new workover and telemetry businesses acquired late in 2009 for which wages and salaries constitute the largest component of cost of services. The total dollar increase was also to a lesser extent attributable to the increase in the dollar/ruble exchange rate.

Fuel and energy costs consist primarily of oil, lubricants and electricity. Fuel and energy costs for 2010 were US $79.5 million, or 6.7% of total cost of services as compared to US $63.6 million, or 7.0% of total cost of services for 2009. The change as a percentage of total cost of services is not material.

Costs relating to the transportation of employees to field locations primarily include transportation services related to the mobilisation and rotation of rig crews. Expenses relating to the transportation of employees to field locations for 2010 were US $23.4 million, or 2.0% of total cost of services as compared to US $28.1 million, or 3.1% of total cost of services for 2009. The change as a percentage of total cost of services is not material.

Leasing and rent costs consist primarily of the cost of renting drilling equipment. Leasing and rent costs for 2010 were US $10.9 million, or 0.9% of total cost of services as compared to US $10.9 million, or 1.1% of total cost of services for 2009. The percentage of total cost of services change is not considered material.

The remaining portion of our cost of services, which we categorise as 'other', includes current repair expenses for fixed assets; license fees; insurance expenses; safety and environmental expenses; and maintenance expenses. Other expenses amounted to US $49.3 million or 4.1% of our total cost of services for 2010, as compared to US $47.8 million or 5.2% of our total cost of services for 2009. The increase in the total amount is primarily caused by the change in the dollar/ruble exchange rate. The decrease in the percentage of total cost of services is considered immaterial.

Selling, general and administrative expenses

Selling, general and administrative expenses increased by US $12.0 million to US $106.9 million for 2010, as compared to US $94.9 million for 2009. The increase is caused by the integration of the acquired in the end of 2009 businesses. As a percentage of total revenues, selling, general and administrative expenses decreased to 5.9% in 2010 from 6.9% in 2009 due to the fixed nature of such expenses.

Taxes other than income taxes

Taxes other than income tax include various local taxes, such as property tax, social tax, education tax, police tax, animal protection tax and small nation's tax. Taxes other than income taxes increased by US $17.4 million to US $72.5 million for 2010 as compared to US $55.1 million for 2009. The increase in taxes other than income taxes was primarily attributable to the integration of the new workover businesses and an increase in the dollar/ruble exchange rate. As a percentage of revenue, taxes other than income taxes were 4.0% for both 2010 and 2009.

Depreciation

Depreciation increased by US $35.6 million to US $142.0 million for 2010 as compared to US $106.4 million for 2009. As a percentage of revenues, the depreciation increased to 7.8% in 2010 from 7.7% in 2009. The total dollar increase was mostly caused by the significant capital expenditures in PP&E during the past 3 years, particularly the acquisition of additional drilling equipment and new drilling rigs that were placed into service in 2009 and 2010, by the depreciation on the equipment and machinery acquired with the purchase of workover and telemetry businesses late in 2009 and by an increase in the dollar/ruble exchange rate. The increase as the percentage of total revenues is not material.

$436m

2010 EBITDA US $436 million

Management's discussion and analysis of financial condition and results of operations continued

Disposal of property, plant and equipment

Gain on the disposal of property, plant and equipment increased by US $5.9 million to US $6.3 million for 2010 as compared to US $0.4 million for 2009. This increase was primarily due to a realised gain on the sale of non-core transportation assets in the Perm region during the first half of 2010.

Income from operating activities

Income from operating activities increased by US $79.8 million to US $294.0 million for the fiscal year 2010, as compared to US $214.2 million for 2009. The increase in total dollars is primarily due to sustained cost control efforts and higher number of metres drilled. As a percentage of revenues, income from operating activities increased to 16.2% in 2010 from 15.5% in 2009. This percentage increase is primarily due to percentage of total revenues decrease in selling, general and administrative expenses as described above.

Interest expense

Interest expense increased by US $1.6 million to US $15.1 million for 2010 as compared to US $13.5 million for 2009. This increase is mostly caused by interest expense on long-term liabilities for PP&E in the workover businesses acquired late in 2009.

Income before income taxes

Income before income taxes increased by US $69.9 million to US $279.2 million for the fiscal year 2010, as compared to US $209.3 million for 2009. The increase in income before income taxes was attributable to the factors described in more detail above.

Income tax expense

Income tax expense increased by US $27.9 million to US $71.8 million for 2010, as compared to US $43.9 million for 2009. In dollar terms, the increase in income tax expense was primarily attributable to the increase in our income. Our effective tax rate increased to 25.7% in 2010 from 20.9% in 2009 primarily due to a 5% foreign withholding tax on certain intercompany dividends declared and paid in the amount of RUR 5.0 billion during 2010 as well as increase in non-deductible expenses. Based on current tax laws, we expect our effective corporate income tax rate to be approximately 23.5% in the future.

Net income

As a result of the foregoing factors, net income increased by US $41.9 million to US $207.4 million for the fiscal year 2010, as compared to US $165.5 million for 2009.

Overview of financial situation as of December 31, 2010 and liquidity

Our balance sheet and cash flows remain strong. Our year-end 2010 financial situation highlights include:

- Cash and cash equivalents as of December 31, 2010 was US $629 million, an increase of US $195 million as compared to cash and cash equivalent balance of US $434 million as of December 31, 2009;
- Our debt as of December 31, 2010 increased to US $404 million as compared to US $182 million debt balance as of December 31, 2009;
- During the fiscal year 2010 we paid dividends in the amount of US $213 million including a US $179 million special dividend on a treasury share sales transaction and a US $34 million dividend resulting from our successful 2009 operations;
- Net cash position (cash reduced by all debt) was US $225 million as of December 31, 2010 (December 31, 2009 net cash position was US $252 million);
- Capital expenditures for the fiscal year ended December 31, 2010 were US $284 million including changes in restricted cash as compared to US $107 million incurred during 2009.

Accounts receivable

Accounts receivable increased by US $44.3 million to US $235.4 million as of December 31, 2010, from US $191.1 million at the beginning of the year. The increase in total dollars is primarily due to increase in revenue. Expressed as the number of days outstanding, our trade receivable balance decreased from approximately 50.7 days at the beginning of the year to approximately 49.3 days at the end of the year (both ratios are expressed in ruble terms). This decrease is due to normal fluctuations in our collection cycle.

04

Strategic focus 04

Expand & improve workover capacity

- June 2010 acquisition of OOO Meridian added 18 workover crews in the Komi Republic, expanding our geographic footprint in the growing Timan-Pechora market
- The Schlumberger transaction (May 2011) added 34 workover and 23 Sidetracking rigs to our fleet, expanding our total workover & sidetracking fleet to over 330 rigs

Materials for drilling and workover

The balance for materials for drilling and workover, a component of our inventory balance, increased by US $17.9 million from US $110.0 million at the beginning of the year to US $127.9 million at the end of the period. Expressed as the number of days for the total inventory to turn over, the turnover rate at the end of the year was approximately 214.0 days, up from 175 days at the beginning of 2010, when expressed in ruble terms. The increase in turnover days as well as the increase in the balance as of December 31, 2010 is primarily attributable to the growth of lower turnover items required for more technologically advanced drilling and higher purchase volumes of spare parts required for maintenance of our rig fleet.

Liquidity and capital resources

The Company's primary sources of liquidity are cash generated from operating activities and debt financing. The Company's plan going forward is to finance its capital expenditures, interest payments and dividends primarily out of operating cash flows as well as to finance a portion of its capital expenditures through existing and prospective future credit facilities.

Cash flows

The table below shows our net cash flows from operating, investing and financing activities for the 12 month periods ended December 31, 2010 and 2009 (in thousands of US dollars, audited):

	2010	2009
Net cash provided by operating activities	**322,553**	409,118
Net cash used in investing activities	**(325,190)**	(125,840)
Net cash provided/(used) in financing activities	**206,188**	(137,059)

Operating activities

Net cash provided by operating activities amounted to US $322.6 million for 2010, as compared to US $409.1 million for 2009. This decrease in cash flows provided by operating activities is principally due to a net negative change in the components of operating assets and liabilities for the fiscal year 2010 compared to 2009. The most significant factor contributing to this change is an increase in accounts receivable and inventory attributed to the overall increase in the volume of the drilling services during 2010 as compared to the contraction of the volume during 2009.

Investing activities

Net cash used in investing activities amounted to US $325.2 million for 2010, as compared to US $125.8 million for 2009. The increase is mostly attributable to our desire to capitalise on the growth opportunities in our markets by significantly increasing our investments in new property, plant and equipment for new projects as well as acquiring new businesses to diversify and expand our service lines.

In 2010 our capital expenditures were US $283.8 million; mainly comprised of US $145.6 million spent on rig fleet upgrade and maintenance, US $61.7 allocated for the new rigs to be delivered in 2011 and US $42 million prepayment for the new build Super 116E jack-up rig.

Financing activities

Net cash provided by financing activities amounted to US $206.2 million for 2010, as compared to net cash of US $137.1 million used in financing activities during 2009. During both years, dividends were paid and principal repayments of long term debt were made. The primary difference between the periods is the result of principal repayments of short term debt and purchase of treasury stock in 2009 as opposed to the sale of all the treasury stock in the first half of 2010 and payment of a special dividend in the approximate amount of the gain generated on the Company's repurchased GDRs. For further details on the transaction, refer to section Overview of other matters. Moreover, in December 2010 we received US $254.3 million from a new credit line for financing strategic acquisitions in 2011.

Liquidity

The table below shows our cash and cash equivalents for the period ended December 31, 2010 and the year ended 2009 (in thousands of US dollars, audited):

	2010	2009
Cash held in banks – mostly in US Dollars	**357,911**	60,000
Short-term deposit – Russian rubles	**154,730**	212,485
Cash held in banks – Russian rubles	**76,451**	44,110
Short-term deposit – US dollars	**40,033**	115,789
Other	**341**	1,340
Total cash and cash equivalents	**629,466**	433,724

Our cash flow in the short term can be negatively affected by the level of expenditures we are required to make in the fourth and first quarters of each year to mobilise our rigs, crews and equipment to drilling sites.

Capital expenditures

Our business is capital intensive and expenditures are primarily required to (i) purchase new drilling rigs and other equipment and (ii) upgrade and modernise the technical characteristics of our existing drilling rigs and equipment. As of December 31, 2010 and 2009 advances given for property, plant and equipment amounted to the following (in thousands of US dollars, audited):

	2010	2009
Advances given for property, plant and equipment	**67,557**	15,779

The amounts represent cash advances for property, plant and equipment not yet received. The increase in advances given for property, plant and equipment is attributable to a US $42 million advance paid for the construction of new jack-up rig to Lamprell.

The table below presents the amounts invested in construction, which is still in progress for the above described periods (in thousands of US dollars, audited):

	2010	2009
Construction in progress	**40,146**	73,997

The decrease in construction in progress in 2010 compared to 2009 is caused by a normal fluctuation in the new drilling rig delivery schedule.

Additionally, as of December 31, 2010, the Company had on deposit restricted cash of approximately US $67.8 million to secure letters of credit opened for the purpose of purchasing new drilling rigs to be delivered in 2011 and to secure a bank guarantee issued for a subcontractor.

Management's discussion and analysis of financial condition and results of operations continued

Capital resources

As of December 31, 2010 and 2009 our short-term and long-term debt amounted to the following (in thousands of US dollars, audited) (please see our 2010 Consolidated Financial Statements and the accompanying notes for more audited):

	2010	2009
Short-term debt and current portion of long-term debt	**117,550**	31,796
Long-term debt	**286,367**	150,379

We believe we have sufficient working capital to meet our requirements for at least the next 12 months. We also expect to meet our contractual payment obligation requirements for at least the next 12 months with cash flows from our operations and other financing arrangements.

Overview of other matters

Dividend policy and year-end 2010 dividend declaration

Our ability to pay dividends depends primarily on the amount of cash we have on-hand and on the receipt of dividends and distributions from our subsidiaries. The payment of dividends by our subsidiaries is contingent upon the sufficiency of their earnings, cash flows and distributable reserves and the ability of our subsidiaries to make, in accordance with relevant legislation, Company law, exchange controls and contractual restrictions, dividend payments and other types of distributions to us.

In August 2007, we adopted a dividend policy according to which we expect to declare and pay dividends each year based on the Company's earnings and the cash needs of the business.

Our results of operations and cash generating capacity continue to be strong which allows us both to invest in our growing business and to increase the dividend payment to our shareholders. The decision of the Board of Directors on the amount of dividends to pay depends on many factors including but not limited to the financial situation and results of the Company, its capital needs for support of business growth, overall macroeconomic and market environment, and tax and legislative issues.

For the year ended December 31, 2010 the dividend was declared by the Board of Directors on December 14, 2010 in the amount of 31 cents per share or US $45 million which was included in 'Accounts payable and accrued liabilities' and paid on January 18, 2011. In 2009 a dividend of 25 cents per share or US $35 million was declared and paid early in 2010.

In addition, on April 15, 2010 the Company announced a one-time special interim dividend of US $1.22 per share which reflected the approximate gain realised by the Group during its buy-back program. Refer to next section for further details.

Treasury shares

In March 2008, the Company introduced an incentive plan for certain members of management for a five year period beginning January 1, 2008. In accordance with its Incentive Compensation Plan (the Plan), 522,060 GDRs were awarded early in 2011 to participants of the Plan for their performance in 2010.

In October 2008, we announced a stock buy-back program in response to the unprecedented reduction in the market price for our shares caused by the virtual collapse of the world-wide credit and equity markets and wholesale rotation out of Russian equities. Between the start of the program and the end of the 2008 we repurchased approximately 9.6 million shares, representing approximately 6.5% of our shares outstanding before the commencement of the program. The repurchase program continued on into the first seven months of 2009 such that by the end of July 2009 we had repurchased a cumulative total of approximately 12.5 million shares of our stock, representing approximately 8.5% of our shares outstanding before the commencement of the program.

Early in 2010 we awarded approximately 718,868 of these GDR's to our officers under the Plan for their performance in 2009.

In April 2010 the remaining treasury shares, net of the award under the Plan and those given to Directors in lieu of cash for their Board service, were successfully placed back in the market using an accelerated book build process. EDC decided to pay a Special Interim Dividend in order for shareholders to benefit from the gain generated on the Company's repurchased GDRs. The size of the Special Interim Dividend was approximately equal to the gain realised by EDC during share buy back program. On April 15 the Special Dividend was announced to be US $1.22 per share or US $179 million. The dividend was paid late May 2010.

Earnings per share

Basic earnings per share is computed by dividing net income available to common stockholders by the weighted-average number of shares of common stock outstanding during the reporting periods. Diluted Earnings per Share reflect shares that may be issued contingent upon stock price performance under the terms of the Plan.

The calculation of earnings per share for the 12 months of 2010 and 2009 was as follows:

	2010	2009
Net income available for common stockholders	**207,353**	165,490
Weighted average number of outstanding shares	**143,270,265**	135,121,647
Basic earnings per share of common stock (US dollars)	**1.45**	1.22
Contingent shares of under the Plan	**522,060**	718,868
Weighted average number of outstanding shares, after dilution	**143,792,325**	135,840,515
Diluted earnings per share of common stock (US dollars)	**1.44**	1.22

Earnings per share calculated on a diluted basis of 143,792,325 shares amounted to US $1.44 in 2010, compared to US $1.22 in 2009. The improvement in earnings per share was attributable mainly to the increase in net income by 25% in 2010 compared to 2009. The weighted average number of shares outstanding increased in 2010 by 6% resulting from placement of the treasury shares bought during 2008 and 2009 (refer to paragraph above) to the market on April 15, 2010.

Basic earnings per share were US $1.45 in 2010 compared to US $1.22 in 2009.

Related party transactions

Shareholder loans

In the period from November 2006 through March 2007, the Company entered into loan agreements with its shareholders to partially fund the investment program of our onshore drilling services division and the purchase of our offshore drilling services business. The aggregate principal amount of such loans was US $70.0 million. The loans mature on December 31, 2011 and incur interest at the rate of 8.6% per annum. In 2010, as well as in 2009, US $6 million dollars was recognised and paid on these loans which are denominated in US dollars. Management believes the terms of these loans are no more onerous than those which would have been negotiated in an arms-length negotiation.

Legal services

The Company's General Counsel, Douglas Stinemetz, is a partner with The Stinemetz Law Firm (the Firm). During 2010 and 2009 the Firm billed EDC for costs and expenses of US $2.2million and US $1.3 million respectively. All services were billed at a discount to the Firm's normal billing rates while expenses were billed at their actual cost. In addition the amounts paid to The Stinemetz Law Firm include considerable third party expenses and charges for the services of other lawyers. Mr. Stinemetz is not otherwise paid for his services as the Company's general counsel. Management believes the amounts paid for these legal services are no more onerous than those which would have been negotiated in an arms-length negotiation for a similar level of service and expertise.

Off-balance sheet arrangements

The Company does not have off-balance sheet arrangements that have, or are reasonably likely to have, a current or future material effect on its financial condition, revenues, expenses, results of operations, liquidity, capital expenditures or capital resources.

Certain factors affecting our results of operations

Changes in crude oil and natural gas prices

The prices of crude oil and natural gas in Russia can have a significant impact on our results of operations. World prices for crude oil are characterised by significant fluctuations that are determined by the global balance of supply and demand. However, Russian natural gas prices are regulated by the Russian government. While Russian natural gas prices have increased in recent years, and are expected to continue to rise to a level closer to parity with export netbacks, they are still significantly below world levels. A substantial or an extended decline in crude oil and natural gas prices could result in lower capital expenditures by our customers, and consequently, a reduction in the number of wells to be drilled by oil and gas companies. Such a pattern of sequential downward and upward changes of our customers' capital expenditures has caused the results of our drilling operations to vary significantly from year to year during the life of the Company. The results of our workover operations tend to be less sensitive to the fluctuations in crude oil and natural gas prices, as our clients require such services both during periods of high and low oil prices.

Change in mix of services

Because margins can vary significantly amongst the services we provide, our results of operations are affected by changes in the mix of onshore and offshore drilling and workover services we provide to our customers. The services we provide in our onshore division have expanded from offering primarily conventional production and exploration drilling services in January 2005 to offering a wider range of higher margin drilling and workover services, including sidetracking, horizontal and underbalanced drilling.

For example, during 2010, we drilled 437 thousand metres utilising the horizontal drilling technique, representing 11% of our total drilling volumes, while in the corresponding period of 2009 our horizontal drilling operations were 337 thousand metres, or about 9% of total drilling volumes. 'Easy to access' reservoirs that were intensively developed during past decades are no longer capable of delivering appropriate flow rates using conventional drilling techniques, though the recovery rate could be further increased. Looking forward we see the increase in horizontal drilling as our customers already enjoyed higher flow rates from the wells drilled horizontally, which if drilled vertically were not economically feasible due too low flow rates. The horizontal drilling technique is especially beneficial when used to drill reservoirs with a greater horizontal dimension rather than vertical thickness. It is estimated that horizontal drilling could improve initial well flow rates by two to seven times in some reservoirs.

Productivity

Our results of operations are affected by the productivity of our crews which in turn depends on a number of factors. Among those factors are crew training and incentives, operating procedures, fleet upgrade and modernisation, logistics flow and mix of services.

Overall, we believe our core productivity per crew was better in 2010 when compared to the same period of 2009. Over the medium-term to long-term we expect our efficiency to continue to improve due to the ongoing implementation and utilisation of more advanced drilling technologies and the application of new standards to our drilling operations. Advanced crew training and application of innovative technologies have allowed us to both improve Rates of Penetration (ROP) and reduce Non-Productive Time (NPT). Examples of technological advancements included wider usage of Polycrystalline Diamond Compact (PDC) drill bits, introduction of new generation drilling motors, optimisation of BHAs and mud programs/properties, and real-time drilling navigation. The use of top-drives and four-step drilling mud cleaning systems on our high specification rigs further improved ROP and efficiency in the increasingly more challenging wells we are drilling.

In 2010 we witnessed a number of factors that could moderate our preferred rate of productivity improvement. All these factors can be broadly described as changing mix of services that we provide to our customers. In 2010 we drilled 30% and 64% more horizontal and exploration wells, respectively, compared to 2009 and exploration and horizontal wells are inherently more time consuming to drill than comparable production wells. Average depth of the wells drilled by EDC in Western Siberia increased in aggregate about 7% over the period of little over two years. Deeper wells require disproportionately more time to drill and heavier drilling rigs. We've also expanded our client base and plan to continue this in the future which, as a general rule, requires rig mobilisations to distant locations. Another factor that affects our crew productivity is seasonality described in more details in the paragraph below.

Seasonality

Our revenue from onshore and offshore drilling services can be negatively affected by severe winter weather conditions in certain regions of Russia that make oil and gas operations difficult to non-operational during that season. For example, during January and February 2010, Russia experienced severely cold temperatures of approximately -45° Celsius in certain regions where we operate and the lost drilling time during such period amounted to approximately 85 days, which was equivalent to the loss of use of three drilling crews for one calendar month, and which contributed to delays in the mobilisation of our equipment and service commencement dates. Our revenue from onshore drilling services may also be negatively affected by spring thawing because drilling rigs, equipment and materials situated in certain regions can only be transported during winter when the ground is sufficiently frozen to create access roads. As a result, a portion of our business activity in the fourth and first quarter of each year is devoted to transportation of drilling rigs, equipment and materials and we experience a decrease in revenues while continuing to incur costs. If we fail to complete a drilling contract on time or are unable to move our equipment due to adverse weather conditions, our ability to timely commence drilling at another site may be impeded. However, the effect of severe weather conditions on our operations depends on the specific type of service being provided. For instance, our onshore exploration drilling services are most affected by adverse weather conditions, as our drilling rigs, equipment, materials and crews that are required for such services are mobilised to remote locations accessible only by winter roads or helicopters. On the other hand, onshore production drilling services tend to be less affected by adverse weather conditions

Management's discussion and analysis of financial condition and results of operations continued

due to the cluster drilling method utilised by us, which involves drilling multiple wells from a single drilling pad. With respect to such drilling method, our operations may be temporarily disrupted by adverse weather conditions in the event we are unable to operate our rigs or mobilise required supplies to rig sites. With respect to our offshore division, we are generally unable to perform drilling services in the Russian and Kazakh sectors of the Caspian Sea during winter months due to the presence of ice. However, the Yuri Korchagin platform is ice-resistant, which allows us to drill there year-round.

Operating capacity

Our revenue growth can be negatively affected by the number of drilling rigs and drilling crews available to us. Our ability to grow our onshore business or maintain its current level depends on our ability to procure a sufficient number of new drilling rigs and modernise our existing ones. Following the stabilisation of the global economy, we witnessed the recovery of the demand for drilling services in Russia. Importantly, since the wells we drill are getting deeper we see the demand coming for heavier rigs; 320 tons or greater. We've developed a five year Plan according to which 18 rigs were ordered in 2010 with delivery times during 2011. The rigs that we are ordering are produced by Russian and Chinese manufactures at prices significantly lower than in 2008 and with much shorter lead times.

At the end of 2010 we believed we had sufficient capacity with the addition of the new rigs added to our drilling fleet and our increased drilling efficiency to drill well over 4.5 million metres on an annual basis. The transactions with Schlumberger and Slavneft will further expand our capacity and strengthen our presence in Russia.

Market trends

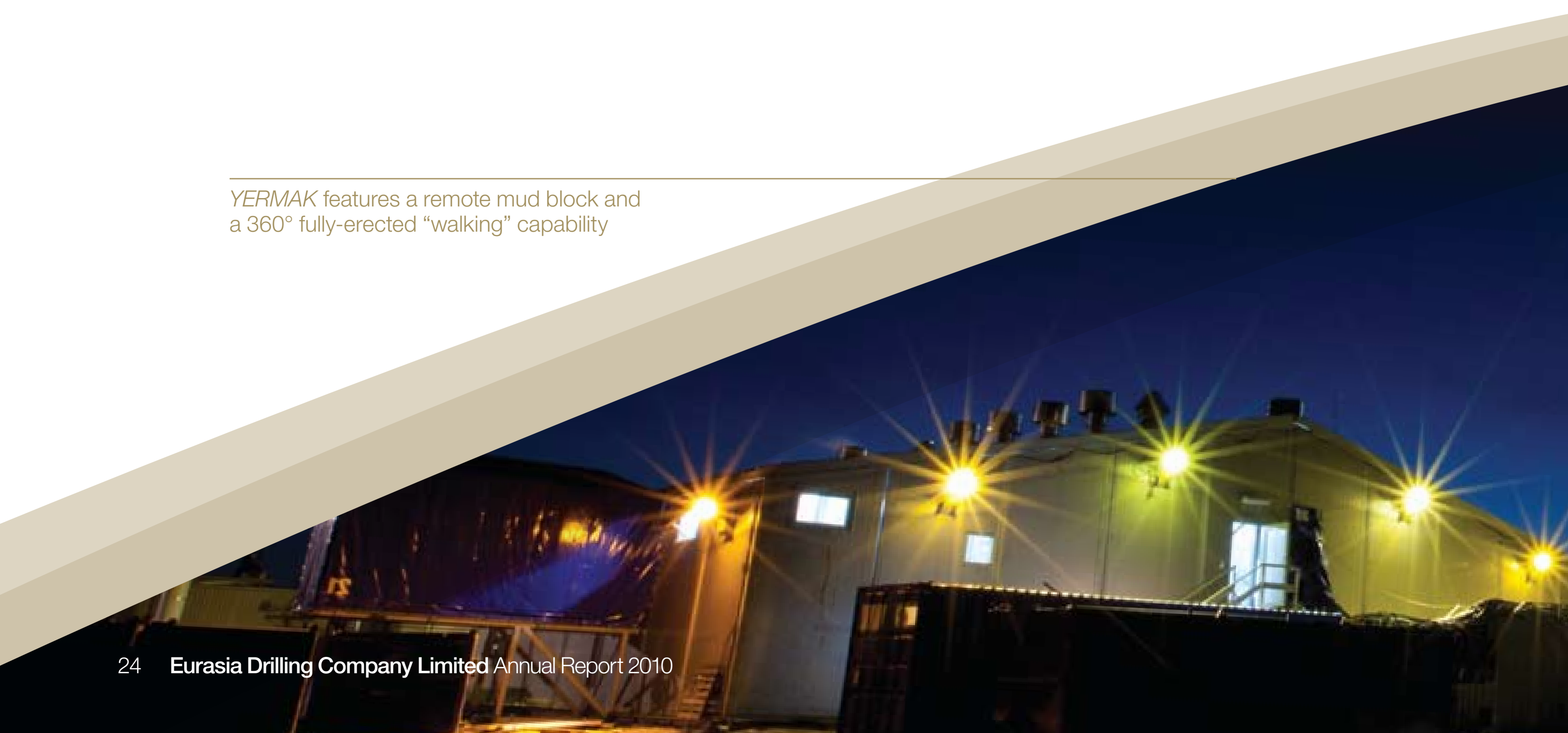
One noticeable recent market trend is a movement by the Russian oil and gas majors to divest themselves of their in-house service divisions. The process of divestment was initiated in 2004 when we acquired substantially all of the onshore drilling and certain related assets of LUKOIL. In 2009 TNK-BP continued the trend by selling its oilfield services assets to Weatherford. In 2010 both Gazpromneft and Slavneft publicly stated their intention to divest their in-house services divisions. Early in 2011, we signed a Letter of Intent to acquire 100% of Slavneft's drilling and exploration assets. It's quite possible that other oil and gas companies will follow this trend in the near future which will change the structure of the oil field services market by shifting activity towards independent providers.

After EDC acquired the onshore drilling assets from LUKOIL in December 2004, drilling volumes in Russia grew at a fairly steady pace through the end of 2007. According to data published by CDU TEK, during the 2005 through 2007 period total metres drilled onshore Russia grew by a Compound Annual Growth Rate (CAGR) of 17.6%. Drilling volume growth slowed in 2008 to 5.7% above 2007 levels. CDU TEK crude oil production figures for Russia show 2.3% CAGR increase in total Russian oil production over the 2005 through 2007 period, and a 0.6% production decline in 2008 v. 2007.

During 2010, CDU TEK data indicated that overall Russian drilling volumes increased by 18% as compared to the corresponding period of 2009, while oil production increased by 2.2% during 2010 versus the corresponding period of 2009. This increase in production was primarily attributable to new Greenfield production that came on-stream in 2009, that compensated for a decrease in Brownfield oil production. As discussed above, seasonality affects drilling operations in Russia, with drilling volumes achieved in the 2nd and 3rd quarters of each year being substantially higher than 1st and 4th quarter levels in a typical year. During 2008, drilling volumes surged more than is typical in the middle portion of the year due to both seasonality effects and the run up in oil prices. During 2009 the seasonal pattern was more modest, but 2010 was characterised by similar seasonality trends as in 2008.

Price optimisation

Our revenue growth depends on our ability to charge clients market prices for our onshore and offshore drilling and other services. The original LUKOIL Framework Agreement, valid from 2005 through 2009, established a pricing adjustment formula applicable to the onshore drilling services we provided to LUKOIL. Such pricing formula effectively limited our ability to adjust the prices related to our onshore drilling services for LUKOIL in order to reflect fluctuations in the market prices occurring prior to the following annual price adjustment. In January 2010 we signed a new Framework Agreement with LUKOIL. More than 50% (excluding additional volumes we will get once we complete transactions with Schlumberger and Slavneft) of our drilling volumes each year is guaranteed on the basis of the Framework



YERMAK features a remote mud block and a 360° fully-erected "walking" capability

Agreement with LUKOIL requiring us to drill a minimum of 6.7 million metres for the period from 2010 to 2012. The pricing formula is similar to the one in the previous Framework Agreement. We consider that the prices at which we provided services pursuant to the LUKOIL Framework Agreement were acceptable given the volume of services provided. In addition, we believe that the contracts we enter into with our other customers provide us with greater flexibility to adjust such contract prices to better conform to current market levels.

Quantitative and qualitative disclosure about market risk

Interest rate risk

Please see our audited consolidated financial statements for 2010 for a description of our short term and long term debt and the associated interest rates and maturities.

Our exposure to market risk for changes in interest rates relates primarily to our long-term and short-term debt. The table below presents scheduled long-term debt maturities in U.S. dollars and related weighted-average interest rates for each of the 12-month periods ending December 31 relating to debt obligations as of December 31, 2010 (in millions, except interest rate percentages). See table below.

As is further described in Note 11 of our December 31, 2010 audited consolidated financial statements, attached elsewhere herein, certain debt was originally contracted at below market interest rates. The schedule above assumes a market rate for such debt in the computation of its fair market value.

Currency risk

We are exposed to foreign currency exchange rate risks. The currency giving rise to these risks is primarily the Russian ruble. We use the Russian ruble for the majority of our operations, while the US dollar is our reporting currency. Foreign exchange gains and losses result from converting monetary and certain non-monetary assets and liabilities denominated in the Russian ruble into US dollar amounts at each balance sheet date. This includes any borrowings in a foreign currency. As of December 31, 2010, we had US $327.5 million of a total of US $403.9 million of our long and short-term debt denominated in the Russian ruble. As of December 31, 2009, we had US $112.2 million of a total of US $182.2 million of our long and short term debt denominated in the Russian ruble. In addition, the results of our operations are impacted by transactions entered into in currencies other than the Russian ruble, and a fluctuation in the Russian ruble/US dollar exchange rates will result in a change in the recognised revenues and expenses associated with such transactions. Furthermore, while the majority of our revenues are denominated in the Russian ruble, some of our costs, including some of those associated with purchases of foreign manufactured land rigs, are denominated in the US dollar and other currencies. Any significant foreign currency exchange rate fluctuations (both short- and long-term) could have a material adverse effect on our business, financial condition and results of operations. In addition, in 2010 certain of our intercompany debt was denominated in a currency other than the functional currency of the debtor company (in all cases the debtor companies are and were 100% owned members of our consolidated group).

Concentration of credit risk

We have a concentration of credit risk since one customer made up approximately 71.2% of our sales during 2010 (68.6% for 2009). In order to reduce the exposure to this credit risk we have been increasing our business with other, unrelated, clients and monitoring our account receivable balances closely. We perform periodic credit checks on our customers and, as a result, did not have any material bad debt expense from our operations during 2010. In 2009 we had a bad debt of approximately $10 million for work performed in prior periods and determined to be uncollectible in 2009. Our Allowance for doubtful accounts stood at US $17.3 million at the end of 2010 (US $18.3 million for 2009), which amount was considered adequate. Our cash and cash equivalents are placed with major banks within Russia, Switzerland and the United Kingdom.

	Scheduled maturity date							Fair value
	2011	2012	2013	2014	2015	2016 and thereafter	Total	Dec 31 2010
Total long term debt	**118.9**	**144.6**	**139.1**	**0.3**	**0.1**	**1.7**	**404.7**	**401.3**
Fixed rate	102.2	127.8	122.3	0.3	0.1	1.7	354.4	351.0
Average interest	8.0%	8.2%	8.2%	0.0%	0.0%	0.0%		
Variable rate[1]	16.7	16.8	16.8				50.3	50.3
Average interest	4.4%	4.4%	4.4%					

1 Based on the LIBOR rate at the end of 2010, which rate may fluctuate in later periods.

05

Strategic focus 05

Broaden technology platform

- EDC transferred our in-house drilling services lines to Schlumberger in early 2011 in exchange for their rig-related assets, and formed a Strategic Alliance in the CIS
- Our Alliance with Schlumberger joins the world's premier service contractor with the largest drilling contractor in the Eastern Hemisphere, providing our clients with best-in-class services for their increasingly complex drilling and workover projects
- In 2010 EDC commissioned its first own-built onshore drilling rig, the 450 metric ton *YERMAK*, which is the most advanced cluster drilling rig in Russia

Corporate responsibility

We continuously seek ways to engage all of our employees in the things occurring in different parts of our organisation.

At EDC we believe that ethical, sustainable and socially responsible operations are fundamental to our business and to our long term growth. It is the way we work.

- We observe and promote ethical business practices and advocate respect and tolerance by and for all people.
- Our business decisions are made to ensure long-term growth for the benefit of our employees, customers and investors.
- We care about where we work and together with our employees, local people and government bodies, we develop constructive solutions to shared problems and promote suitable projects and initiatives that are of long-term benefit to the local communities.
- We are committed to high standards in occupational health and safety and to protecting the environment.

Commitment to our People

With more than eighteen thousand employees we are focused on providing them with a safe and high quality working environment backed up by a first class compensation and benefits package. In addition, we have a 'Collective Bargaining Agreement' that governs social and labor relations for more than 80% of our workforce.

One of the key components of employees' social protection is the supplementary pension plan provided by LUKOIL-Garant, a non-state pension fund to which we contribute on behalf of our employees.

For a company like ours, with a significant number of employees spread over the vast territories of Russia and the CIS, it is important to keep open channels of communication. We continuously seek ways to engage with our employees regarding matters occurring across the business. Our news directory contains news from our subsidiaries and is available to each employee to keep them informed of ongoing developments. We have also initiated an employee survey to identify the degree of satisfaction of our employees and to define areas for improvement. We are pleased with the results of this survey as the vast majority of our employees indicated they are generally satisfied and would recommend EDC as an employer. The results were published internally and we continue to improve communication channels with our employees.

We place special emphasis on developing young specialists. An annual contest held by EDC identifies young, creative employees and supports their development while encouraging innovative projects. The best projects of prior years are now implemented within EDC's operations.

In 2010 the young specialists contest was hosted by our West Siberia branch. 15 contestants presented their projects covering various aspects of EDC operations and business activities, including environmental responsibility. The first prize was awarded to a project analysing ways to improve the commercial speed of drilling by implementation of a more efficient drilling bit hydraulic horsepower program. Winners and all contestants received monetary prizes, certificates and souvenirs.

On an annual basis the Ministry of Energy of the Russian Federation and the NS 'Integraziya' Society organise a contest for the best youth projects covering Russia's oil and energy sector issues. Winners of the 2010 EDC competition took part in a national contest in May 2010, and five projects out of six submitted were awarded prizes. One of the projects, covering aspects of more efficient use and modernisation of cementing units, was awarded a certificate from the Ministry of Energy of the Russian Federation.

We have established Youth Boards to help improve our young employees' social life and communicate their concerns to the management of the Company. We have also introduced a counsellor-counsellee system where our young specialists are mentored by senior employees to help them achieve their potential.

Commitment to HSE

Our 140 strong HSE group promotes our Health, Safety and Environmental Protection policies and procedures to all our employees and works to ensure that we comply with all government laws and regulations.

We are a member of the International Association of Drilling Contractors (IADC) to which we regularly report our HSE statistics. Historically, since 2005, our lost time incident rate (LTIR) was lower than the worldwide industry indicator reported by the IADC. We are happy to report that this trend continued in 2010 as our LTIR was 0.19 compared to 0.38 for the industry as reported by the IADC. Most importantly, there were no fatal incidents in 2010.

In September 2008, BKE, our Russian onshore operating subsidiary, received compliance certificates for ISO 14001:2004 (Environmental Protection Management System) and OHSAS 18001:2007 (Health and Safety Management System). In September 2010, a surveillance audit was carried out by the Bureau Veritas Certification, an independent certification body, and BKE was recertified as compliant with the requirements of the above mentioned standards.

In June 2007, BKE Shelf, our offshore operating subsidiary, was audited and recognised as complying with the Quality Standard ISO 9001:2000 (Russian Register Certification System) under the IQNET program. Early in 2010 BKE Shelf was audited and recognised as complying with the revised Quality Standard ISO 9001:2008.

The minimisation of any negative effects of our operations on the environment is critical to us. Our offshore operations in the Caspian Sea are in strict compliance with the zero discharge principle. This principle means that no waste is discharged into the sea; rather it is collected in closed containers and transported onshore for disposal. The zero discharge principle is applied during all of our exploration and production drilling.

Commitment to the Community

We are involved in several projects in various communities where we operate, aimed at improving the wellbeing of the local population. Our support includes financial assistance for the disabled, low-income families, disabled and elderly war veterans, and disadvantaged, disabled and orphaned children.

The charities we supported in 2010 included the Government of Russia Charity Fund, to which we provided financial assistance in arranging holidays for disabled children, and to publish special books for the blind. We took part in the charity event 'Not Only Kids', organised by the 'All Together Charity Fund'. We contributed to the 'Here and Now Orphan Charity' fund's 'Holidays out of home' event for children from patronage families. We cooperate with 'Pomogi.org', a charity fund which addresses childrens' urgent medical needs, providing financial assistance for medical treatment for children with cerebral paralysis. We also support specialty schools, including a boarding school in Travino Settlement and the 'Ulitka' Rehabilitation Center for teenage girls, both in Astrakhan.

EDC supports the development of youth sport in the regions of our operations, and we strive to enrich the cultural life of the communities. As an example, we sponsor the local national holidays for the Khanty-Mansiysk and Yamalo-Nenetz Autonomus Regions population.

We have a long-standing cooperation with many educational institutions to provide internships for students at our facilities. In 2010 we provided over 400 places for university and college students. Educational institutions involved include: Kostroma State Technical University, Ufa State Aviation and Technical University, Orenburg State University (Buguruslansk branch), Tyumen State University, Ufa State Oil and Technical University, Tyumen State Oil and Gas University, Saratov State University of N.G. Chernyshevsky, Zhirnovsk Oil College, Samara State Technical University, Perm State Technical University, SPO Ishimbaisk Oil College, Perm Oil College, Perm State University, Tchaikovsky Industrial and Humanitarian College, Osa Agricultural College, Russian State University of Gubkin, Volgograd Academy of Government Service, the Modern Humanitarian Academy of Volgograd, Irkutsk State Technical University, North-Caucasus State Technical University and Uhta State Technical University.

Commitment to our investors and customers

We do all this while never losing sight of the fact that, fundamentally, we are here to run a successful business that makes a profit and invests for continued long-term growth.

We are focused on improving the liaison with our shareholders and analysts in an open and efficient way. We put our efforts into ensuring that our stakeholders are well informed on our strategy, outlook, financial and operational performance in a timely manner.

During the year we provide four financial and operations updates including annual and interim results. We report our drilling volumes on our web site (www.eurasiadrilling.com) to keep our investors and analysts informed on the direction of our business on a monthly basis.

We understand and recognise the importance of our investors' opinions and feedback, which we collect during numerous investor meetings. As such, in 2010 we held over 200 one-on-one and group meetings and attended eleven investor conferences, including two Global Energy Conferences involving our Chief Operating Officer and Chief Financial Officer. We conducted three investor non deal road shows covering Russia, USA, UK and Europe through the course of the year.

Our Investor Relations section on our website provides additional information, including investor presentations, annual reports, calendar of events and other useful information.

0.19LTIR

EDC's Lost Time Incident Rate in 2010, as compared to 0.38 for the industry (IADC)

Board of Directors

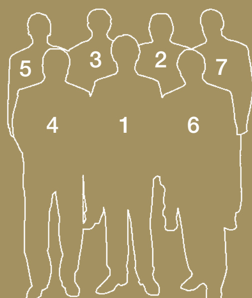
1. The Earl of Clanwilliam
Chairman of the Board of Directors of EDC

The Earl of Clanwilliam has been Chairman of the EDC Board of Directors since October 2007. He has been a member of the Board of Directors of OJSC Polyus Gold since March 2006. Earl of Clanwilliam founded and is currently a director of The Policy Partnership Limited. Since 1997, Earl of Clanwilliam has served as a member of the Board of Directors of the Benevolent Society of St. Patrick, and since 2005, he has served on the Advisory Council of the Ukrainian British City Club. Earl of Clanwilliam is a graduate of Eton College.

2. Dr. Alexander Djaparidze
Chief Executive Officer of EDC

Dr. Djaparidze is one of the founders of EDC and has been CEO of the Company since August 2007. Dr. Djaparidze has been a member of the Board of Directors of BKE since 2005 where he served as the Chairman from 2005 until present. From June 1995 to February 2007, Dr. Djaparidze served as President of PetroAlliance. Dr. Djaparidze holds a degree in Mining Engineering and Geophysics from the Gubkin Russian State University of Oil and Gas. Dr. Djaparidze is a Candidate of Technical Science from the Gubkin Moscow Institute of Oil and Gas.

Dr. Djaparidze was awarded the Russian Federation Government prize for special achievements in science and technology.



3. Alexander Shokhin

Mr. Shokhin has been a member of the Board of Directors of EDC since October 2007. He has been a member of the Board of Directors of LUKOIL and Chairman of its Personnel and Remuneration Committee since January 2005. He is also a member of the Board of Directors of TNK-BP since February 2009. Mr. Shokhin has been the President of the State University-Higher School of Economics since 1995. He also has been President of the Russian Union of Industrialists and Entrepreneurs since 2005.

Mr. Shokhin is a Doctor of Economic Science, Professor and Member of the Russian Academy of Natural Sciences. He was awarded the Order of Honor (1997) and the State Order 'For Merits before the Fatherland' of 4th degree (2008).

4. Victor Kalyuzhniy

Mr. Kalyuzhny has been a member of the Board of Directors of EDC since September 2009. Mr. Kalyuzhny recently retired from the position of Extraordinary and Plenipotentiary Ambassador of the Russian Federation in the Republic of Latvia. From 2000 to 2004 Mr. Kalyuzhny was Russia's Deputy Foreign Minister and Special Presidential Representative for Caspian Sea Status Settlement. Mr. Kalyuzhny graduated from Ufa Oil Institute.

5. Martin Hansen

Mr. Hansen served as our Chief Financial Officer from May 1, 2004 until November 17, 2007 and has served as a member of our Board of Directors of EDC since January, 2005. He was formerly a member of the Board of Directors of BKE from 2005 to 2007. From 1999 to 2002, Mr. Hansen was Chief Financial Officer of PetroAlliance. Mr. Hansen holds a Bachelor of Business Administration degree from the University of Iowa.

6. Richard Matzke

Mr. Matzke has been a member of the Board of Directors of EDC since September 2010. He has been a member of the Board of Directors of LUKOIL from 2002 until mid-2010, and was re-elected in 2011. From 2000, Mr. Matzke served as Vice-Chairman of the Board of Chevron until his retirement in 2002 after 41 years of service at the company. Previously, Mr. Matzke was Vice-President of Chevron and President of Chevron Overseas Petroleum Inc. from 1990 until 1999.

Mr. Matzke was Awarded a non-Government (sectoral) medal "For Development of the Russian Oil & Gas Industry" in 2006. Mr. Matzke graduated from Iowa State University (1959), Pennsylvania State University (1961), and St. Mary's College in California (1977). Richard Matzke has both a BS and Masters in Geology, an MBA degree and he has also received an honorary doctorate.

7. Rene Huck

Mr. Huck has been a member of the Board of Directors of EDC since October 2007. Mr. Huck retired from Schlumberger in October 2005 where he held a variety of senior positions over 15 years, most recently as Vice-President QHSE and Industry Affairs. Mr. Huck has been a member of the Board of Directors of BW Offshore, an FPSO company, since 2006, and also served on the Board of Directors of PetroAlliance from 2004 to 2007. Mr. Huck is a Mechanical Engineer from Ecole Centrale in Nantes, France and a Petroleum Engineer from the French Petroleum Institute in Paris, France.

Corporate governance report

The Company is committed to observing high standards of corporate governance. This report describes how the Company has applied the Principles of Good Governance as set out in the Combined Code on Corporate Governance, issued by the UK Financial Reporting Council in June 2008 (the 'Combined Code'), except where indicated otherwise within this report. While the Company as a legal entity incorporated in the Cayman Islands is not subject to UK corporate governance requirements per se, the Company nevertheless intends to comply with established practices under the UK Combined Code, wherever reasonably possible.

The Board

The Board of Directors of the Company consists of seven Directors. Six out of the seven members of the Company's Board of Directors serve in a non-executive capacity. Dr. Djaparidze, the seventh Director, is also the Company's Chief Executive Officer. The Board considers five of these six non-executive Directors (Earl Clanwilliam (formerly Lord Gillford), who also serves as Chairman, Mr. Huck, Mr. Matzke, Mr. Hansen and Mr. Kalyuzhny) to be independent for purposes of the Combined Code.

One non-executive Director, Mr. Shokhin, is not strictly independent for the purposes of the Combined Code, since he is also a member of the board of directors of two customers of the Company, LUKOIL and TNK-BP. Nevertheless, the Board does not consider that this fact undermines his independence. In fact, the Board considers that, as a result of his service on these other boards, he brings particular expertise to the Company's Board of Directors since he has a greater industry specific knowledge.

The Board considers and will continue to consider its composition from time to time. The Remuneration and Nomination Committee of the Board on March 1, 2009 has adopted a policy as to how best consider and nominate members of the Board. The Board may choose to deviate from the strict requirements of the Combined Code in relation to Board composition on a case-by-case basis if it is considered in the best interests of the Company, consistent with industry practice generally or required by applicable Cayman Islands law.

In accordance with the Articles of Association, the Company's Board of Directors is divided into three classes. Each Director holds his office for a term of three years, such terms being staggered in accordance with resolutions adopted at the Company's Annual General Meeting held September 9, 2009. The initial terms of the initial Board of Directors of each class expire at the annual general meeting of Shareholders:

Class I, which comprises two Directors, expired and was re-elected in 2009; Class II, which comprises two Directors, expired and was re-elected at the Annual General Meeting of the Shareholders in 2010; and Class III, which comprises three Directors, expires and will be submitted for re-election at the Annual General Meeting of the Shareholders in October 2011. At each Annual General Meeting of the Shareholders of the Company, one class of directors will be elected for a full term of three years to succeed that class of directors whose terms are expiring. The three year cycle relating to the appointment and tenure of each class of directors referred to above is a continuous rolling cycle, commencing for the second time in the year following the third year of the cycle. Shareholders may only appoint or remove directors at such time in the cycle as they are due for re-election.

Mr. Martin Hansen was re-elected as Class I Director on September 11, 2009. Mr. Albert Vladimirov stepped down as Class I Director on September 11, 2009, and the Annual General Meeting of the Shareholders elected Mr. Victor Kalyuzhny as Class I Director on the same day.

Mr. Rene Huck was re-elected as Class II Director on September 16, 2010. Mr. Todd Gremillion stepped down as Class II Director on September 16, 2011, and the Annual General Meeting of Shareholders elected Mr. Richard Matzke as Class II Director on the same day.

Name	Age	Position	Expiration of term
Earl of Clanwilliam	49	Chairman of the Board of Directors	2011
Alexander Yu. Djaparidze	55	Director	2011
Martin E. Hansen	69	Director	2012
Rene Huck	63	Director	2013
Victor Kalyuzhny	64	Director	2012
Richard Matzke	73	Director	2013
Alexander Shokhin	59	Director	2011

Brief biographies of the executive and non-executive Directors are set out on page 29. The biographies illustrate that the Directors have a range of business and financial experience that is important and relevant to the management of the Company. The role of Chairman of the Board and Chief Executive Officer are clearly defined and separate.

Except as otherwise noted, each member of the Board of Directors was appointed to the Board on October 15, 2007.

Information on Board meeting attendance

During 2010 the Company's Board of Directors held four meetings, on March 12, 2010, June 25, 2010 (Todd Gremillion attended by proxy granted to Dr. Djaparidze), October 16, 2010 and December 14, 2010. All the Board members attended all four meetings, either in person, by proxy or by telephone. The overall attendance rate by Directors was 100%.

Information on Board authority

The Company is controlled through its Board. The Board's main roles are to manage the Company with the objective of maximising shareholder value, setting the general business strategy of the Company and overseeing the decision-making and risk management processes within the Company. The Board is governed by its Charter, which is posted on the Company's web site.

The Board reserves to itself certain key matters to approve or monitor, such as the Company's business plans, annual budget, significant capital expenditures, as well as the Company's operating and financial performance. The Directors are provided with regular information on the Company's performance and activities and meet on a regular basis. Meetings include a formal schedule of matters specifically reserved for the Board's decision. Additional special meetings of the Board may be called as necessary.

As required by the Combined Code, all Directors have access to the advice and services of the Company Secretary, and any Director wishing to do so in furtherance of his duties may take independent professional advice at the Company's expense. In the year ended 31 December 2010, no Director, except Mr. Huck, sought independent professional advice. Mr. Huck employed the services of a professional firm in the valuation of compensation for the purposes of the Nomination and Remuneration Committee's evaluation of the Company's compensation structure. In order to discharge their duties, Directors are provided with access to papers prior to Board meetings and Directors are free to seek any further information they consider necessary. In addition, between Board meetings, Directors have access to the Company's officers and employees in order to progress the Company's business.

In order to facilitate the Directors' fulfilment of their responsibilities regarding continuing education and to enhance each Director's knowledge of the Company, the Company's business operations and the latest developments in corporate governance, the management provides Directors with the following:

- access to, or notice of, continuing educational programs that are designed to keep Directors abreast of the latest developments in corporate governance matters and critical issues relating to the operation of public company boards;
- material that contains information pertaining to (i) the Company's industry and (ii) comparisons of the Company with its major competitors; and
- reports and presentations from various advisors of the Company on its business.

Chairman and Chief Executive

There is a clear division of responsibilities between the Chairman and the Chief Executive Officer. The Chairman is responsible for leadership of the Board, ensuring its effectiveness in all aspects of its role, setting its agenda and implementing the Board's resolutions, as well as for coordination of operational activities with the Chief Executive Officer with an objective of delivering value to the shareholders. The Chief Executive Officer is responsible for formulating strategy and for ensuring its delivery once agreed upon by the Board. The Chief Executive Officer is appointed by the Board to manage the Company and to supervise and hold accountable all EDC operations personnel. The Chief Executive Officer has authority on all matters of management and is accountable for all duties and responsibilities delegated by the Board for the performance of the Company. The Chief Executive Officer is primarily responsible for new business development, communicating with shareholders and analysts and all other areas of day-to-day management of operations of the Company. In doing so, he works with the executive management team, which comprises Vice Presidents and certain other senior executives.

Board evaluation

The Board of Directors conducted an annual self-evaluation to determine whether it and its Committees were functioning effectively. The assessment was discussed with the full Board at its meeting. The assessment focused on consideration and discussion of the Board's contribution to the Company; the nature and level of its interaction with the Company's management; the quality, quantity and scope of information which flows to the Board from management, and the way in which it flows; the content of Board meetings and presentations to Board meetings; the practical arrangements for the work of the Board; the work and operation of the Board's Committees; and the areas in which the Board or management believes that the Board could improve. Overall, Board members concluded that the Board and its Committees were operating in an effective and constructive manner.

Insurance
In accordance with provision A1.5 of the Combined Code, the Company has in place Directors' and Officers' Insurance in respect of the Directors' duties as directors.

Board committees
The principal committees of the Board are the Audit and Finance, Remuneration and Nomination and Corporate Governance Committees. We believe that our Audit and Finance Committee serves the same function as the audit committee recommended by the Combined Code and that our Remuneration and Nomination Committee serves the same function as the remuneration committee and the nominations committee recommended by the Combined Code. We are not currently able to comply with the requirements of the Combined Code in relation to the composition of the audit committee and the remuneration committee. Our Audit Committee is comprised of four members: Earl Clanwilliam, the Chairman, Mr. Huck (both commencing in July 2010), Mr. Hansen, our former Chief Financial Officer, all of whom are non-executive Directors, independent for purposes of the Combined Code, and Mr. Shohkin, who, although a non-executive Director, is not strictly independent for purposes of the Combined Code. Our Remuneration and Nomination Committee is comprised of four members, Dr. Djaparidze, our Chief Executive Officer, and Earl Clanwilliam, the Chairman (commencing in July 2010), Mr. Kalyuzhny and Mr. Huck, who are non-executive Directors and are independent for purposes of the Combined Code. We will seek to modify the composition of our Audit and Finance Committee and our Remuneration and Nomination Committee over time as further appointments are made to our Board of Directors.

Each of the Committees has Terms of Reference under which authority is delegated by the Board. The Terms of Reference for each Committee can be found at: www.eurasiadrilling.com/corporate-governance.html

The Board delegates specific responsibilities to Committees as described below.

Audit and Finance Committee
The Company's Audit and Finance Committee consists of four members: Earl Clanwilliam, Mr. Shokhin, Mr. Hansen and Mr. Huck. The Committee is chaired by Mr. Shokhin. The Audit and Finance Committee convenes as often as necessary. The Committee is authorised to carry out the following functions relating to the control of the Company's financial and business operations:

- coordinate with the Company's independent auditors and prepare recommendations for its Board of Directors in connection with the election and removal of the independent auditors and on the fee and scope of services to be provided by the independent auditors;
- assess the independent auditors' reports;
- review the Company's standards and internal controls procedures and make appropriate reports and recommendations to the Company's Board of Directors;
- assess the Company's financial reports;
- review and approve budgets and business plans, as well as the process for developing budgets and business plans;
- review and approve intercompany financings; and
- review and approve any financing transactions with a value in excess of US $50 million.

Remuneration and Nomination Committee
The Company's Remuneration and Nomination Committee consists of four members: Earl of Clanwilliam, Mr. Huck, Mr. Kalyuzhny and Dr. Djaparidze. The Committee is chaired by Mr. Huck. The Committee is responsible for establishing and implementing a policy for the compensation of directors, consultants and members of senior management, which may take the form of cash, stock options granted pursuant to stock option plans and other benefits. More detailed information about the Remuneration and Nomination Committee is given in the Remuneration report on pages 38–40.

Corporate Governance Committee
Our Corporate Governance Committee consists of two members: Earl of Clanwilliam and Mr. Matzke, who replaced Mr. Gremillion in September 2010. The Committee is chaired by Earl of Clanwilliam. The Corporate Governance Committee is responsible for assisting and advising our Board of Directors with respect to matters relating to the general operation of the Board of Directors, our corporate governance and the performance of the Board of Directors and individual directors.

To ensure compliance with the Company's obligations under the Listing Rules (including the obligations under the Disclosure and Transparency Rules) of the United Kingdom Listing Authority (UKLA), to preserve the Company's reputation for integrity and ethical conduct and to avoid improper conduct by anyone associated with the Company, the Company introduced a Corporate Disclosure Policy and a Share Dealing Policy. The Company has also established a Disclosure Committee. More detailed information about the Corporate Disclosure and Share Dealing Policies, and the Disclosure Committee is given in the Remuneration report on pages 38–40.

Relationship with shareholders

The Company continues to increase its communication with shareholders, investors and brokers. Presentations are made to analysts, the press and institutional investors at the time of the announcement of the full year and half-year results. The Company, principally through the Chief Executive Officer, Chief Financial Officer and Vice President Marketing and Investor Relations maintains a regular dialogue with institutional shareholders and financial analysts, particularly following the interim and preliminary results announcements.

The Company has an internet web site www.eurasiadrilling.com on which it publishes its press releases, Stock Exchange announcements, announcements of conference calls with shareholders and other information concerning the Company's business and upon which it also publishes its annual and interim results. The Annual General Meeting is the principal forum for dialogue with private shareholders. Shareholders may obtain copies of Annual and Interim Reports upon request. A business presentation is made by the Chief Executive Officer and there is an opportunity for shareholders to put questions to the Directors.

Internal controls

The Board is responsible for the Company's system of internal controls and for reviewing its effectiveness. However, such a system can only manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable, but not absolute, assurance against material misstatement or loss.

The Board maintains full control over strategic, financial, operational and compliance issues. Within the overall objectives set by the Board, the management of the Company is delegated to the Chief Executive Officer, who is assisted by the Company's management. The responsibilities of the Company's management include:

- the development and recommendation of strategic plans for consideration and approval by the Board that reflect the longer-term objectives and priorities established by the Board;
- implementation of the strategies and policies of the Company as determined by the Board;
- monitoring of the operating and financial results against the plans and budgets;
- prioritising the allocation of technical and human resources;
- developing and implementing risk management systems; and
- managing and monitoring health, safety and environmental matters.

In addition, the Company's policies contain a statement on business conduct, which emphasises the legal, ethical and moral standards that have to be employed in all of the Company's business dealings. The Company expects the highest standards from all employees and key suppliers.

Statement of compliance with the Combined Code

The Directors believe the Company has complied with the provisions set out in the Combined Code, except as set out above in this report. The Directors are of the opinion that these areas of noncompliance do not prejudice shareholders' interests and is justifiable given the specific circumstances of the Company.

Going concern

The Directors are satisfied that the Group has adequate resources to continue to operate for the foreseeable future and have adopted the going concern basis in preparing the financial statements.

Greater than five percent shareholdings

As of December 31, 2010, the following are shareholders who, to the Company' knowledge, own, directly or indirectly, greater than five percent (5%) of the Company's issued and outstanding shares. The percentages below are based upon the amount of authorised and issued shares of the Company as at December 2010, less the number of shares of the Company bought by a wholly owned subsidiary of the Company under Incentive Compensation Plan in the end of 2010.

Alexander Djaparidze	42.65%*
Alexander Putilov	22.96%
Serik Rakhmetov	8.20%

*Dr. Djaparidze is also CEO and a member of the Board of Directors of the Company. His shareholding includes shares owned by Cloudburst Orange Limited and Margin Finance Company Limited.

Results of 2010 Annual General Meeting of shareholders

On September 16, 2010, the Company held its annual shareholders' meeting in Cannes, France. The primary business brought before the meeting consisted of three proposals. The first proposal sought to amend the Company's Articles of Association to clarify certain aspects of Board service, namely authorising the Board to declare an annual dividend as appears to the Board of Directors to be justified. The second proposal sought re-election and appointment of Class II Directors. The third proposal sought shareholder approval of the appointment of KPMG as the Company's independent accountant.

The first proposal was approved by about 94% of the shares voting, while the other two were passed by about 98% of the shares voting. Approximately 82% of the total issued and outstanding shares of the Company voted at the meeting either in person or by proxy.

Auditor's fees for 2010

The Company's independent auditing firm is ZAO KPMG, a company incorporated under the laws of the Russian Federation and a member firm of the KPMG network of independent member firms affiliated with KPMG International, a Swiss cooperative. During 2010 the Company paid ZAO KPMG US $1,451,984 (net of VAT) for auditing services. The firm provided no material non-audit services to EDC during 2010.

Statement of Directors' responsibilities in respect of the Annual Report and the financial statements

The Directors are responsible for preparing the Annual Report and the Company financial statements in accordance with applicable law and regulations.

Our corporate affairs are governed by our amended and restated memorandum of association (the 'Memorandum of Association'), the amended and restated articles of association (the 'Articles of Association') and by the Companies Law (2010 Revision) (the 'Companies Law') and the common law of the Cayman Islands. As noted in the Corporate Governance Report, because the Company is incorporated in the Cayman Islands, it is not subject to UK corporate governance requirements. Because the Company intends to comply with established best practice, wherever possible and where it is in the Company's interests, the Company has applied the Principles of Good Governance as set out in the Combined Code, except where indicated within this report.

The Company's Audited Consolidated Financial Statements and the accompanying notes have been prepared in accordance with US GAAP.

In preparing the Company's financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgments and estimates that are reasonable and prudent;
- state whether they have been prepared in accordance with US GAAP; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The Directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that its financial statements comply with the US GAAP. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the group and to prevent and detect fraud and other irregularities.

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's web site. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other applicable or controlling jurisdictions.

To the best of the Directors' knowledge:

(a) The Financial Statements prepared in accordance with US GAAP give a true and fair view of the assets, liabilities, financial position and profit-loss of the Company and its consolidated undertakings; and

(b) The Annual Report includes a fair review of the development and performance of the Company's business and the position of the Company and its consolidated undertakings as a whole, together with a description of the principal risks and uncertainties they face.

Directors' report

This Report is submitted for the year ended December 31, 2010.

Activities, profits and dividends

The principal activities of the Company continue to be the onshore and offshore drilling services in Russia and in the Caspian Sea, as well as onshore integrated well construction and workover services. The Company's profit for the year amounted to US $207.4million (2009: US $165.5 million).

For the year ended December 31, 2010 the Board of Directors declared an ordinary dividend on December 14, 2010 in the amount of 31 cents per share or US $45 million which was included in 'Accounts payable and accrued liabilities' and paid on January 18, 2011. In 2009 a dividend of 25 cents per share or US $35 million was declared and paid early in 2010. In addition, on April 15, 2010 the Company announced a one-time special interim dividend of US $1.22 per share or US $179 million which reflected the approximate gain realised by the Group during its buy-back program. Refer to the Corporate Governance report on pages 30–34 for further details.

Further descriptions of the Company's development and performance during the year, position at the year end and likely future prospects are reviewed in the Chairman's Statement, the Chief Executive's Statement, in the Management's discussion and analysis of financial condition and results of operations on pages 12–25, the Corporate governance report on pages 30–34, and the Remuneration report on pages 38–40, which are incorporated into this Directors' report as if set forth herein.

Share Capital and Major Shareholders

The Company's Share Capital and Major Shareholders are set forth in the Notes to consolidated financial statements on pages 53–71 the Corporate governance report on pages 30–34 and the Remuneration Report on pages 38–40.

Retirement and re-election of Directors

In accordance with the Articles of Association, the Company's Board of Directors is divided into three classes. Each Director holds his office for a term of three years, such terms being staggered in accordance with resolutions adopted at the Company's Annual General Meeting held September 9, 2009. Pursuant to the Articles of Association, one-third (rounded down) of the Directors of the Company are required to retire by rotation at each Annual General Meeting (AGM). The retiring Directors are eligible to stand for re-election.

At the 2010 AGM, Class II Directors, Mr. Rene Huck and Mr. Todd Gremillion, retired by rotation. Mr. Huck stood for re-election and was re-elected as Class II Director on September 16, 2010. Mr. Todd Gremillion stepped down as Class II Director on September 16, 2011, and the Annual General Meeting of Shareholders elected Mr. Richard Matzke as Class II Director on the same day.

Company policies

The Directors have adopted several policies applicable to the Directors, officers and employees of the Company including:

Corporate Disclosure Policy summary

The Company has adopted a Corporate Disclosure Policy, a copy of which is available on the Company's web site.

The Corporate Disclosure Policy regulates the disclosure of information about the Company to the public. The purpose of the Policy is to raise awareness of the Company's approach to disclosure among the Board of Directors, senior management and employees of the Company. This Corporate Disclosure Policy does not derogate from the Company's existing policies and practices regarding confidential information.

A disclosure committee (the 'Disclosure Committee') has been established with responsibility for overseeing the Company's disclosure practices and consists of the Chief Executive Officer, Chief Financial Officer and General Counsel of EDC. Confidential information about or related to the Company must not be disclosed to third parties except in accordance with the Corporate Disclosure Policy. The Corporate Disclosure Policy provides examples of what may constitute confidential information, which depending upon the circumstances may include, but are not limited to the following: (i) changes in corporate structure; (ii) changes in capital structure; (iii) changes in financial results; (iv) changes in business operations; (v) acquisitions and dispositions; and (vi) changes in credit arrangements.

Share Dealing Policy summary

The Company has adopted a Share Dealing Policy, a copy of which is available on the Company's web site.

The Share Dealing Policy forbids dealing in the Company's shares based on material non-public information, i.e. insider trading and similar offenses. The purpose of the Share Dealing Policy is to ensure compliance with the law, to preserve the Company's reputation for integrity and ethical conduct and to avoid improper conduct by anyone associated with the Company. The Share Dealing Policy makes the Company's Directors, officers and employees aware that they are all personally responsible for ensuring the Company's strict compliance with this Policy and that any breach of it will be treated as a disciplinary offence with the severest consequences. The Policy establishes certain procedures and requires all persons to consult with the General Counsel of the Company before taking any action that may be covered by the Policy.

Policy and practice on payment of suppliers

As a result of the nature of the Company's business, its contractual relationships with suppliers of goods and services and with sub-contractors vary according to circumstances. It is the Company's policy to enter into an appropriate form of contractual agreement on payment terms and to pay according to those terms. The Company does not follow any particular code or practice for the payment of creditors. In practice, the Company makes every effort to pay accordingly when it can be confirmed that the supplier has provided the goods or services in accordance with the relevant terms of the contract.

Significant agreements

The Directors are not aware of any significant agreements to which the Company and/or any of its subsidiaries or associates is a party that take effect, alter or terminate upon a change of control of the Company following a takeover bid, save that a subsidiary that ceased to be a subsidiary of the Company would cease to benefit from the Company's financing arrangements.

Annual General Meeting

The Directors have scheduled an Annual General Meeting of the Members of the Company for October 25, 2011 in Florence, Italy. Details of the resolutions to be proposed at the Annual General Meeting are given in the Notice of Annual General Meeting, which is published separately and sent to shareholders. The Directors consider that all of the resolutions set out in the Notice of Annual General Meeting are in the best interests of the Company and its shareholders as a whole and recommend that shareholders vote in favour of each of them.

Amendments to the Articles of Association

As adopted by resolutions of the Annual General Meeting of Shareholders held September 16, 2010, the Company amended and restated its Articles of Association as follows:

'1. Article 108 will read: 'The Board of Directors may declare an annual dividend, as appears to the Board of Directors to be justified'.

Auditors

During the year KPMG Limited remained as the Company's independent auditors. KPMG Limited have expressed their willingness to continue in office. Accordingly, a resolution to reappoint KPMG Limited as the Company's independent auditor will be proposed the forthcoming Annual General Meeting.

Remuneration report

This Remuneration Report for the year ending December 31, 2010 sets out how the principles of the UK Combined Code of Corporate Governance (the 'Combined Code') relating to Directors' and senior management remuneration are applied. The Board believes that the Company was generally compliant with the provisions of the Combined Code relating to management remuneration throughout the period, except where indicated within this Report.

Remuneration of the Board of Directors

Board member remuneration for the Company consists of a cash stipend plus reimbursement for each director's actual expenses incurred in attending the Company's Board meetings. The cash stipend paid to each Board member for 2010 was as follows:

Name	Amount
Earl of Clanwilliam	$121,875
Alexander Djaparidze	$112,500
Alexander Shokhin	$112,500
Martin Hansen	$112,500
Todd Gremillion[1]	$79,829
Rene Huck	$121,875
Victor Kalyuzhny	$112,500
Richard Matzke	$28,125

1 Replaced September 16, 2010. Mr. Gremillion is currently an advisor to the Board.

At its December 2008 Board meeting the Board adopted a policy by which Board members could elect to receive the value of their yearly cash stipend in shares of the Company's stock, valued at the previous year-end closing price. Certain of the directors chose this option for 2010. Non-executive Directors do not receive any performance-related bonuses, pensions, share options or other forms of benefit. The Board may grant extra remuneration to any Director who performs special services at the request of the Company. No such extra remuneration was granted in 2010.

Remuneration Committee

The Board has delegated to the Remuneration and Nomination Committee, through Terms of Reference, consideration of executive remuneration issues generally, including the use of share incentive plans. The Remuneration and Nomination Committee comprises of four members: Rene Huck (Chairman), a non-executive director whom the Company deems independent, Earl Clanwilliam, Chairman and nonexecutive director whom the Company deems independent, Victor Kalyuzhny, a nonexecutive director whom the Company deems independent, and Alexander Djaparidze, a director who is also the Company's Chief Executive Officer. (Dr. Djaparidze does not vote on his own compensation.) The Committee effective January 1, 2009 approved an amendment to the award plan under the Company's 2007 Incentive Compensation Plan to provide for awards solely in the shares of the Company. The terms of reference permit the Remuneration Committee to obtain its own external advice on any matter at the Company's expense.

Remuneration policy for executive Directors and senior management

The objective of the Company's remuneration policy is to ensure that executive directors and members of the senior management of the Company are provided with appropriate incentives to encourage enhanced performance and are, in a fair and responsible manner, rewarded for their individual contributions to the success of the Company. Dr. Djaparidze, the Company's Chief Executive Officer, is the sole executive director. The Committee aims to provide a competitive remuneration package to attract, retain and motivate senior management with the experience needed to shape and execute the Company's strategy and deliver shareholder value. The Committee takes account of external market data supplied by independent professional advisers and is sensitive to the wider scene, including pay and employment conditions elsewhere in the Company, especially when determining annual salary increases.

The Committee's policy is for a significant proportion of executive reward to be variable and dependent upon the Company's performance. Variable reward components provide an opportunity for higher levels of remuneration where this remuneration is supported by exceptional performance, whether at an individual level or in relation to the Company's short-term and longer-term business priorities. Variable rewards will continue to be provided through a balanced mix of performance-related elements. The annual bonus scheme supports operational objectives over the financial year, whilst the Company's schedule of awards under its 2007 Incentive Compensation Plan will reward superior performance over a longer period.

The remuneration of senior management consists of:

- Basic salary – which forms the major element of remuneration and is based on comparable positions in leading businesses of similar size and complexity.
- Annual discretionary bonus – which is based on achievement of Company profit targets, as well as other financial and non-financial measures and personal targets. The maximum bonus payout is fifty percent (50%) of salary.
- 2007 Incentive Plan – under which the senior management may receive awards in an aggregate value of up to fifteen times (15x) each such person's annual salary and bonus, depending upon the increase in the price of the Company's GDRs over five years, payable in shares of the Company.

Further details of each element of the senior management's remuneration package, together with details of interests in shares, are set out below in this report.

Information on compensation of the Company's top five officers

The following table sets forth compensation for the Company's five most highly compensated officers employed on a full-time basis during 2010. In addition to the amounts set forth below, the Company reimburses its officers for their actual out-of-pocket expenses incurred while conducting the Company's business. Does not include benefits under the Company's Incentive Compensation Plan, if any.

Name	Title	Total compensation paid in 2010
Alexander Djaparidze	CEO-EDC	$1,068,763
W. Richard Anderson	CFO-EDC	$1,050,000
Taleh Aleskerov	Sr. VP Finance-BKE	$696,283
Alexander Bogachev	President-BKE	$501,950
Vadim Bayanov	Sr. VP Operations-BKE	$378,336

Management remuneration

(a) Basic salary and benefits

The Company structures remuneration packages which are appropriate to the particular function and level of responsibility of each individual member of senior management and which are designed to attract, retain and motivate such persons. It takes into account the remuneration structures and levels at other companies, in particular in the Russian oilfield services sector. Eligible members of senior management are also provided with insurance and other health benefits in accordance with market standards.

Senior management compensation for the period January 1, 2010 through December 31, 2010 in the aggregate was approximately US $3,689,332.

(b) Annual discretionary bonus scheme

The Company operates an annual discretionary bonus scheme under which eligible members of management are able to earn a discretionary bonus up to a maximum of fifty percent (50%) of salary, dependent upon performance conditions being met. The bonus is payable in cash.

Senior management discretionary bonuses for the period January 1, 2010 through December 31, 2010 in the aggregate was approximately US $1,650,000.

(c) Share incentive plan

It is the Remuneration and Nomination Committee's policy that senior management should participate in the Company's Incentive Compensation Plan as this scheme aligns their interests with those of our shareholders by linking the reward available to participants with increase in the overall price of the Company's GDRs. Details of the share incentive awards are set out below.

2007 Incentive Compensation Plan

In July 2007, the Board of Directors considered and approved the 2007 Incentive Compensation Plan (the 'Plan'). The Plan was adopted by the Board of Directors to reward certain corporate officers, directors and key employees of the Company and certain independent consultants by enabling them to acquire ordinary shares of the Company and/or other awards as the Remuneration and Nomination Committee of the Board of Directors deems appropriate. The Plan was designed to attract and retain key employees of the Company and its subsidiaries, to attract and retain qualified directors of the Company, to attract and retain consultants and other independent contractors and to stimulate the active interest of such persons in the development and financial success of the Company and its subsidiaries. The Plan allowed the Company to issue ordinary shares in the Company up to five percent (5%) of the total ordinary shares issued and outstanding on such terms and conditions as are, in the best judgment of the Board of Directors, necessary, appropriate, advisable or convenient in connection with the foregoing.

In March 2008, the Remuneration and Nomination Committee approved a schedule of awards under the Plan, similar to a phantom stock plan. Under this schedule of awards, eligible members of senior management are granted an opportunity during the period beginning January 1, 2008 and ending December 31, 2012 (the 'Performance Period') to earn incentive compensation awards (individually an 'Award' and collectively – 'Awards') in an aggregate value of up to fifteen times (15x) each such participant's annual compensation, meaning each participant's annual salary and bonus, calculated for each calendar year beginning January 1 and ending December 31 ('Award Year') within the Performance Period based on the participant's current salary and bonus at the Starting Date for such Award Year ('Annual Compensation'). Starting Date means the date one year prior to the last trading day on the London Stock Exchange prior to the end of the applicable Award Year (the 'Target Date'). Each Award Year, the Award is an amount equal to the participant's respective Annual Compensation times fifteen (x15) multiplied by the applicable Annual Available Award Percentage for the Award Year and then multiplied by the applicable Annual Award Percentage Reached for the Award Year. Annual Available Award Percentage means a percentage set forth in the table below, indicating how much Annual Compensation is available for an Award each Award Year if a Target Price Increase (i.e. percentages listed below for target increases in the Company's GDR price each Award Year) is realised. Annual Award Percentage Reached means the percentages set forth below, indicating what percentage of the available Annual Compensation shall be granted as an Award each Award Year if an applicable Target Price Increase is realised.

Pursuant to the Incentive Plan, the terms and conditions of each Award are to be set forth in an award agreement between the participant and the Company, incorporating the terms of the Incentive Plan and its Exhibits. Awards may be earned by the participants each Award Year upon the Company's GDR price reaching certain Target Price Increases. No such Award is to be made if such Target Price Increases are not achieved. The Target Price Increase achieved in any Award Year will be calculated based on the percentage increase of (i) the average sale price per GDR, quoted by the LSE, for the twenty (20) trading days preceding the Target Date over (ii) the Starting Price.

Column A of the table below sets out five (5) possible Target Price Increases for each Award Year of the Performance Period. Column B states the Annual Award Percentage Reached upon achievement of the applicable Target Price Increase for such Award Year.

Column A	Column B
Target Price Increase Reached	**Annual Award Percentage**
Below 5% increase in the Starting Price	0%
From 5% up to 10% increase in the Starting Price	25%
From 10% up to 15% increase in the Starting Price	50%
From 15% up to 20% increase in the Starting Price	75%
From 20% or more increase in the Starting Price	100%

The Award will be made in un-equal instalments each Award year during the Performance Period in accordance with the table below, in which (i) Column C represents the applicable Award Year and (ii) Column D represents the Annual Available Award Percentage of Annual Compensation available to calculate the Award in such Award Year.

Column C	Column D
Award Year Percentage	**Annual Available Award**
2008	12%
2009	15%
2010	18%
2011	25%
2012	30%
Total	**100%**

Each participant's right to such Award vests on the earliest of (i) the calendar day which is immediately after the applicable Target Date, provided that the participant on that date is still employed or otherwise in good standing with the Company and/or its affiliates. The Company will pay the participant such Award within thirty (30) days of the date it vests (the 'Payment Date').

If a participant's employment with the Company or its affiliates is terminated on or prior to a Target Date or such participant is deemed not in good standing as may be determined by the Company from time to time in its sole discretion on or prior to a Target Date, such participant will forfeit any Award and shall have no right to receive any Award arising on such Target Date.

The Remuneration and Nomination Committee approved the award of 522,060 GDRs to Plan participants for their performance in 2010. One GDR represents one ordinary share.

Interests of Directors and senior management in the Company

As of December 31, 2010, the Directors and certain senior management of the Company, to the Company's best knowledge, had the following interests in shares of the Company:

Directors and senior management	Shares (including GDRs)	Percentage of shares
Alexander Djaparidze[1]	62,442,899	42.65%
Martin Hansen	165,790	0.11%
Alexander Bogachev	136,820	0.09%
Taleh Aleskerov	98,532	0.07%
W. Richard Anderson	45,095	0.03%
Vadim Bayanov	42,684	0.03%
Doug Stinemetz[2]	10,167	0.01%

1 Alexander Djaparidize is a Director, as well as our Chief Executive Officer. Alexander Djaparidize was the beneficial owner of an aggregate of 62,442,899 shares. Alexander Djaparidize owned directly 2,716,307 shares. Alexander Djaparidize was a beneficial owner of 33,192,340 shares through his beneficial ownership of Cloudburst Orange Limited. A familial trust of Alexander Djaparidze was a beneficial owner of 26,489,172 shares, which included 1,570,000 shares through its ownership of Margin Finance Company Limited.

2 S. Douglas Stinemetz, our General Counsel and Secretary, was a beneficial owner of 10,167 shares through his ownership of Eagle Eye Holdings, Inc.

As of December 31, 2010, no other Directors, to the Company's best knowledge, had interests in shares in the Company. As of December 31, 2010, there were no options or other commitments to issue additional shares in the Company apart from any disclosed above.

Independent auditors' report

The Board of Directors
Eurasia Drilling Company Limited
We have audited the accompanying consolidated balance sheets of Eurasia Drilling Company Limited and its subsidiaries as of December 31, 2010 and 2009, and the related consolidated statements of income, stockholders' equity and comprehensive income, and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Eurasia Drilling Company Limited and subsidiaries as of December 31, 2010 and 2009, and the results of their operations and their cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

ZAO KPMG
April 19, 2011

Consolidated balance sheets

as of December 31, 2010 and 2009
(all amounts in thousands of US dollars, unless otherwise noted)

	Note	2010	2009
Assets			
Current assets			
Cash and cash equivalents	3	**629,466**	433,724
Accounts receivable, net	4	**235,360**	191,054
Inventories	5	**145,633**	116,801
Taxes receivable	12	**34,960**	35,772
Deferred income tax assets	12	**11,407**	11,227
Other current assets		**20,241**	6,271
Total current assets		**1,077,067**	794,849
Property, plant and equipment	6	**765,184**	684,188
Long-term accounts receivable	7	**6,838**	4,013
Deferred income tax assets	12	**1,422**	277
Goodwill	17	**32,727**	30,792
Other non-current assets	8	**70,830**	9,289
Total assets		**1,954,068**	1,523,408
Liabilities and stockholders' equity			
Current liabilities			
Accounts payable and accrued liabilities		**258,706**	228,499
Advances received		**20,295**	37,239
Short-term debt and current portion of long-term debt	10	**117,550**	31,796
Deferred income tax liabilities	12	**478**	–
Taxes payable	12	**54,257**	53,463
Total current liabilities		**451,286**	350,997
Long-term debt	11	**286,367**	150,379
Accrued pension liability	13	**6,889**	3,865
Deferred income tax liabilities	12	**24,744**	16,009
Total liabilities		**769,286**	521,250
Stockholders' equity	16		
Common stock		**1,469**	1,469
Treasury stock, at cost		**(13,148)**	(58,332)
Additional paid-in capital		**691,535**	528,163
Retained earnings		**578,989**	596,340
Accumulated other comprehensive loss		**(74,063)**	(65,482)
Total stockholders' equity		**1,184,782**	1,002,158
Total liabilities and stockholders' equity		**1,954,068**	1,523,408

W. Richard Anderson
CFO of Eurasia Drilling Company Limited
April 19, 2011

Consolidated statements of income

for the years ended December 31, 2010 and 2009
(all amounts in thousands of US dollars, unless otherwise noted)

	Note	2010	2009
Revenues			
Drilling and related services		**1,798,881**	1,362,222
Other sales and services		**13,275**	19,981
Total revenues		**1,812,156**	1,382,203
Cost of services	15	**(1,195,891)**	(912,050)
General and administrative expenses		**(106,920)**	(94,861)
Taxes other than income taxes		**(72,547)**	(55,061)
Depreciation		**(142,000)**	(106,390)
Gain on disposal of property, plant and equipment		**6,344**	382
Goodwill impairment loss	17	**(7,096)**	–
Income from operating activities		**294,046**	214,223
Interest expense		**(15,125)**	(13,524)
Interest income		**7,993**	10,631
Currency transaction loss		**(7,355)**	(4,414)
Net gain on acquisitions of businesses	17	**557**	2,849
Other expenses		**(951)**	(418)
Income before income taxes		**279,165**	209,347
Income tax expense	12	**(71,812)**	(43,857)
Net income		**207,353**	165,490
Basic earnings per share of common stock (US dollars)		**1.45**	1.22
Diluted earnings per share of common stock (US dollars)		**1.44**	1.22

Consolidated statements of stockholders' equity and comprehensive income

for the years ended December 31, 2010 and 2009
(all amounts in thousands of US dollars, unless otherwise noted)

	Common stock	Treasury stock, at cost	Additional paid-in capital	Retained earnings	Accumulated other comprehensive income/ (loss), net of tax	Total Stockholders' equity
Balance as of December 31, 2008	**1,469**	**(40,100)**	**519,763**	**464,461**	**(65,050)**	**880,543**
Comprehensive income:						
Net income	–	–	–	165,490	–	**165,490**
Other comprehensive income:						**–**
Foreign currency translation loss	–	–	–	–	(2,592)	**(2,592)**
Pension benefits:						
Prior service benefit	–	–	–	–	1,483	**1,483**
Actuarial gain	–	–	–	–	677	**677**
Comprehensive income	–	–	–	–	–	**165,058**
Purchase of treasury stock	–	(18,621)	–	–	–	**(18,621)**
Disposal of treasury stock	–	389	–	–	–	**389**
Incentive compensation plan	–	–	8,400	–	–	**8,400**
Dividends declared	–	–	–	(33,611)	–	**(33,611)**
Balance as of December 31, 2009	**1,469**	**(58,332)**	**528,163**	**596,340**	**(65,482)**	**1,002,158**
Comprehensive income:						
Net income	–	–	–	207,353	–	**207,353**
Other comprehensive income:						**–**
Foreign currency translation loss	–	–	–	–	(7,510)	**(7,510)**
Pension benefits:						
Prior service cost	–	–	–	–	(1,535)	**(1,535)**
Actuarial gain	–	–	–	–	464	**464**
Comprehensive income	–	–	–	–	–	**198,772**
Disposal of treasury stock	–	54,956	162,548	–	–	**217,504**
Purchase of treasury stock	–	(13,148)	–	–	–	**(13,148)**
Incentive compensation plan	–	–	4,200	–	–	**4,200**
Exercise of incentive compensation plan	–	3,376	(3,376)	–	–	**–**
Dividends declared	–	–	–	(224,704)	–	**(224,704)**
Balance as of December 31, 2010	**1,469**	**(13,148)**	**691,535**	**578,989**	**(74,063)**	**1,184,782**

Consolidated statements of cash flows

for the years ended December 31, 2010 and 2009
(all amounts in thousands of US dollars, unless otherwise noted)

	Note	2010	2009
Cash flows from operating activities			
Net income		**207,353**	165,490
Adjustments for non-cash items:			
Depreciation		**142,000**	106,390
Accrued interest expense		**2,893**	1,185
Deferred income taxes		**8,767**	(493)
Gain on disposal of property, plant and equipment		**(6,344)**	(382)
Loss on disposal of subsidiary		**391**	–
Goodwill impairment loss	17	**7,096**	–
(Decrease) increase in allowance for doubtful accounts receivable		**(947)**	11,184
Foreign currency exchange rate difference (unrealised)		**3,862**	4,917
Incentive plan		**4,200**	4,200
All other items – net		**(485)**	501
Changes in operating assets and liabilities:			
Accounts receivable		**(41,080)**	34,579
Inventories		**(27,383)**	61,564
Taxes receivable		**3,197**	1,646
Other current assets		**(6,646)**	13,920
Accounts payable and accrued liabilities		**42,015**	(32,100)
Advances received		**(16,839)**	27,967
Taxes payable		**(1,351)**	5,175
Other current liabilities		**1,854**	3,764
Net cash provided by operating activities		**322,553**	409,507
Cash flows from investing activities			
Purchases of property, plant and equipment		**(224,970)**	(176,608)
Change in restricted cash	8	**(58,807)**	69,793
Proceeds from sale of property, plant and equipment		**8,190**	4,349
Sale of subsidiary		**767**	–
Loans issued		**(7,238)**	–
Acquisition of subsidiaries, net of cash acquired		**(43,132)**	(23,374)
Net cash used in investing activities		**(325,190)**	(125,840)
Cash flows from financing activities			
Principal repayments of short-term debt		**–**	(45,366)
Proceeds from issuance of long-term debt		**255,193**	–
Principal repayments of long-term debt		**(40,037)**	(35,207)
Repayment of capital lease obligations		**(538)**	(3,927)
Dividends paid		**(212,786)**	(34,327)
Proceeds from sale of treasury stock		**217,504**	–
Purchase of treasury stock		**(13,148)**	(18,621)
Net cash used in financing activities		**206,188**	(137,448)
Effect of exchange rate changes on cash		**(7,809)**	8,075
Net increase in cash and cash equivalents		**195,742**	154,294
Cash and cash equivalents at beginning of period		**433,724**	279,430
Cash and cash equivalents at end of period	3	**629,466**	433,724
Supplemental disclosures of cash flow information			
Interest paid		**11,910**	13,090
Income tax paid		**57,145**	44,991

Notes to consolidated financial statements

(all amounts in thousands of US dollars, unless otherwise noted)

Note 1. Organisation and environment

The primary activities of Eurasia Drilling Company Limited (the 'Company') and its subsidiaries (together, the 'Group') include providing exploratory and developmental drilling and oil and gas field services to companies operating within the Russian Federation, Kazakhstan, and the Caspian Sea region.

Eurasia Drilling Company Limited was registered on November 25, 2002 under the Law of the Cayman Islands. The Company was established for the purpose of acquiring OOO LUKOIL Burenie and its subsidiaries.

In November 2004 Eurasia Drilling Company Limited entered into a purchase agreement with OAO LUKOIL to acquire OOO LUKOIL Burenie and its subsidiaries. The acquisition was completed on December 30, 2004. Prior to the acquisition, the Company had no operating activity.

OOO LUKOIL Burenie, now OOO Burovaya Kompaniya Eurasia, was established in accordance with the decision of the Board of Directors of OAO LUKOIL as of February 13, 1995 and registered by the resolution of the Head of Kogalym Administration No 216 as of May 17, 1995. It was formed from the West Siberian drilling subdivisions of OAO LUKOIL.

As of December 31, 2010 and 2009 OOO Burovaya Kompaniya Eurasia had on-shore operating branches in Kogalym, Perm, Usinsk and Zhirnovsk (Volgograd Region) in the Russian Federation.

In 2007 the Group established a subsidiary in Kazakhstan, TOO BKE Kazakhstan Burenie, to provide on-shore drilling services.

In December 2006, the Group acquired a 100% interest in LUKOIL Shelf Limited and LUKOIL Overseas Orient which provide off-shore drilling services in the Caspian Sea to various oil and gas companies in the Russian Federation, Kazakhstan and Turkmenistan. In 2007 these companies were renamed EDC Shelf Limited and AstraOrient Limited, respectively. In 2007, the Company established a Russian subsidiary, OOO BKE Shelf, to operate its off-shore drilling services segment. All operations from EDC Shelf Limited were transferred to OOO BKE Shelf.

In December 2009, the Group acquired a 100% interest in OOO Tekhgeoservice (OOO TGS), a Russian provider of wellsite directional drilling and telemetry services (refer to Note 17).

In December 2009, the Group acquired a 100% interest in OOO Kogalym Well Workover Division (OOO KWWD) and OOO Urai Well Workover Division (OOO UWWD) which provide well workover, well reconditioning and well servicing operations in West Siberia (refer to Note 17).

In June 2010, the Group acquired a 100% interest in OOO Meridian which performs workover in Komi region (refer to Note 17).

In August 2010 the Group acquired a 100% interest in OOO 'Megionskoye Tamponazhnoye Upravleniye' (OOO MTU), a provider of cementing services in West Siberia (refer to Note 17).

The majority of the Group's revenues are currently derived from services provided to OAO LUKOIL and its affiliated entities (the 'LUKOIL Group') and as such, the Group is economically dependent upon its contractual agreements with the LUKOIL Group (refer to note 21).

Business and economic environment

The Russian Federation, Kazakhstan, and Turkmenistan have been experiencing political and economic change that has affected, and may continue to affect, the activities of enterprises operating in these countries. Consequently, operations in these countries involve risks that may not exist in other markets.

The accompanying financial statements reflect management's assessment of the impact of the business environment in the countries in which the Group operates on the operations and financial position of the Group. The future business environment may differ from management's assessment.

Basis of preparation

The consolidated financial statements have been prepared by the Group in accordance with accounting principles generally accepted in the United States of America ('US GAAP').

Note 2. Summary of significant accounting policies

The following significant accounting policies have been applied in the preparation of the consolidated financial statements.

Principles of consolidation

These consolidated financial statements include the financial position and results of the Company and controlled subsidiaries of which the Company directly or indirectly owns more than 50% of the voting interest, unless minority interest shareholders have substantive participating rights. Other significant investments in companies of which the Company directly or indirectly owns between 20% and 50% of the voting interest and over which it exercises significant influence but not control, are accounted for using the equity method of accounting. Investments in other companies are recorded at cost. Equity investments and investments in other companies are included in 'Other non-current assets' in the consolidated balance sheet.

Use of estimates

The preparation of the consolidated financial statements requires management of the Group to make a number of estimates and assumptions relating to the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of revenues and expenses during the reporting period. Significant items subject to such estimates and assumptions include the carrying amount of property, plant and equipment, goodwill impairment assessment, accounts receivable, inventories, deferred income taxes, long-term debt, accrued pension liability and stock-based compensation liability. Actual results could differ from those estimates.

Acquisitions

Assets acquired and liabilities assumed in business combinations are recorded on the Company's consolidated balance sheet as of the respective acquisition dates based upon their fair values at such dates. The results of operations of the businesses acquired by the Company begin to be included in the Company's consolidated statement of income upon the respective acquisition dates.

Functional and reporting currency

The functional currency of the Company and its subsidiaries, except for OOO Burovaya Kompaniya Eurasia, OOO Kliver, OOO NTS, OOO TGS, OOO KWWD, OOO UWWD, OOO Meridian, OOO MTU and TOO BKE Kazakhstan Burenie, is the US dollar. The functional currency of OOO Burovaya Kompaniya Eurasia, OOO Kliver, OOO NTS, OOO TGS, OOO KWWD, OOO UWWD, OOO Meridian and OOO MTU is the Russian ruble and the functional currency of TOO BKE Kazakhstan Burenie is the Kazakh Tenge because these are the currencies of the primary economic environments, in which they operate and in which cash is generated and expended. The Group's reporting currency is the US dollar.

Translation from the functional currency to the US dollar was conducted as follows:

- all assets and liabilities were translated from the functional to the reporting currency at the exchange rate effective at the reporting date;
- equity items were translated from the functional to the reporting currency at the historical exchange rate;
- items in the statement of income and cash flows were translated from the functional currency to the reporting currency at rates, which approximate rates at the date of transaction.

Translation differences resulting from the use of these exchange rates are included as a separate component of accumulated other comprehensive income.

The closing exchange rate as of December 31, 2010 and 2009 was 30.4769 and 30.2442 Russian rubles to one US dollar, respectively.

The Russian ruble and other currencies of republics of the former Soviet Union are not readily convertible outside of their countries. Accordingly, the translation of amounts recorded in these currencies into US dollars should not be construed as a representation that such currency amounts have been, could be or will in the future be converted into US dollars at the exchange rate shown or at any other exchange rate.

Cash and cash equivalents

Cash and cash equivalents include all highly liquid investments with an original maturity of three months or less.

Cash with restrictions on immediate use

Cash funds for which restrictions on immediate use exist are accounted for within other current or non-current assets. The group classifies restricted cash in other current assets if the cash is to be used within a year for payment of existing or maturing obligations. If the cash is to be held for a longer period of time, the restricted cash is shown in the other non-current assets. Cash classification in the noncurrent section is also set aside for plant expansion, retirement of long-term debt or purchase of long-term investments.

Accounts receivable

Accounts receivable are recorded at their transaction amounts less allowance for doubtful accounts. Allowance for doubtful accounts receivable is recorded to the extent that there is a likelihood that any of the amounts due will not be obtained. Non-current receivables are discounted to the present value of expected cash flows in future periods using the original discount rate.

Note 2. Summary of significant accounting policies continued

Inventories

Inventories, consisting primarily of materials and tools used for drilling are stated at the lower of cost or market value. The cost of inventories is determined using an 'average cost' method.

Property, plant and equipment

Property, plant, and equipment are stated at cost, net of depreciation. Depreciation is calculated on a straight-line method over the useful lives of the assets, estimated to be in the following ranges:

Buildings	15–30 years
Machinery and equipment	2–20 years
Vehicles	5–10 years

The cost of maintenance, repairs and replacement of minor items of property, plant and equipment is expensed as incurred. Major renewals and improvements of assets are capitalised.

Goodwill

Goodwill represents the excess of the cost of an acquired entity over the net of the amounts assigned to assets acquired and liabilities assumed. It is assigned to reporting units as of the acquisition date. Goodwill is not amortised, but is tested for impairment at least on an annual basis and between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. The impairment test requires estimating the fair value of a reporting unit and comparing it with its carrying amount, including goodwill assigned to the reporting unit. If the estimated fair value of the reporting unit is less than its net carrying amount, including goodwill, then the goodwill is written down to its implied fair value.

Impairment of long-lived assets

Long-lived assets and certain intangible assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset group may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset group to the estimated undiscounted future net cash flows expected to be generated by that group. If the carrying amount of an asset group exceeds its estimated undiscounted future net cash flows, an impairment charge is recognised by writing down the carrying value to the estimated fair value of the asset group. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to dispose and are no longer depreciated.

Leased assets

Leases under which the Group assumes substantially all the risks and rewards of ownership are classified as capital leases. Leased property, plant and equipment meeting certain capital lease criteria are capitalised and the present value of the related lease payments is recorded as a liability. Amortisation of capitalised lease assets is computed on the straight-line method over the estimated useful life.

Payments for operating leases, under which the Group does not assume all the risks and rewards of ownership are expensed in the period they are incurred.

Income taxes

Deferred income tax assets and liabilities are recognised for the future tax consequences attributable to temporary differences between the carrying amounts of existing assets and liabilities for the purpose of consolidated financial statements and their respective tax bases and operating loss and tax credit carry forwards. Deferred income tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred income tax assets and liabilities of a change in tax rates is recognised in the consolidated statement of income in the reporting period which includes the enactment date.

The ultimate realisation of deferred income tax assets is dependent upon the generation of future taxable income in the reporting periods in which the originating expenditures become deductible. In assessing the realisability of deferred income tax assets, management considers whether it is more likely than not that the deferred income tax assets will be realised. In making this assessment, management considers the scheduled reversal of deferred income tax liabilities, projected future taxable income, and tax planning strategies.

An income tax position is recognised only if the uncertain position is more likely than not of being sustained upon examination, based on its technical merits. A recognised income tax position is measured at the largest amount that is greater than 50% likely of being realised. Changes in recognition or measurement are reflected in the period in which the change in judgment occurs. The Company records interest and penalties relating to unrecognised tax benefits in income tax expense in the consolidated statements of income.

Note 2. Summary of significant accounting policies continued

Interest-bearing borrowings

Interest-bearing borrowings are recognised initially at cost. Subsequent to initial recognition, long-term borrowings are stated at amortised cost with any difference between cost and redemption value being recognised in the consolidated statement of income over the period of the borrowings.

If borrowings are repurchased or settled before maturity, any difference between the amount paid and the carrying amount is recognised in the consolidated statement of income in the period in which the repurchase or settlement occurs.

Pension benefits

The expected costs in respect of pension obligations of the Group are determined by an independent actuary. The net periodic costs are recognised as employees render the services necessary to earn the postretirement benefits.

Environmental expenditures

Group companies accrue for losses associated with environmental remediation obligations, when such losses are probable and reasonably estimable. Such accruals are adjusted as further information becomes available or circumstances change.

Revenue recognition

Drilling and related services

Drilling and related services are generally sold based upon contracts with customers that do not include significant post-delivery obligations. Service revenue is recognised when the services are rendered and collectability is reasonably assured. Rates for services are typically priced on a per day, per metre, per man-hour, or similar basis. Claims and change orders that are in the process of being negotiated with customers for extra work or changes in the scope of work are included in revenue when collection is deemed probable to the extent that the work has been performed.

The Group uses the units-of-delivery method (a modification of the percentage-of-completion method) of accounting for contracts. The units-of-delivery method recognises as revenue the contract price of units of a basic production product delivered during a period and as the cost of earned revenue the costs allocable to the delivered units; costs allocable to undelivered units are reported in the balance sheet as inventory or work in progress.

Revenue is recognised only when it is probable that the economic benefits associated with the transaction will flow to the Group.

Other sales and services

Revenues for other sales and services are recognised when the significant risks and rewards of ownership have passed to the buyer, when it is probable that economic benefits will flow to the Group and when these economic benefits can be reliably measured.

All sales are shown net of value added tax.

Treasury stock

Purchases by Group companies of the Company's outstanding stock are recorded at cost and classified as treasury stock within Stockholders' equity. Authorised and Issued stock includes treasury stock. Outstanding stock does not include treasury stock.

Earnings per share

Basic earnings per share is computed by dividing net income available to common stockholders by the weighted-average number of shares of common stock outstanding during the reporting period. A calculation is carried out to establish if there is potential dilution in earnings per share if convertible securities were to be converted into shares of common stock or contracts to issue shares of common stock were to be exercised. If there is such dilution, diluted earnings per share are presented.

Share-based payments

The Group accounts for liability classified share-based payment awards to employees at fair value on the date of grant and as of each reporting date. Expenses are recognised over the vesting period. Equity classified share-based payment awards to employees are valued at fair value on the date of grant and expensed over the vesting period.

Note 2. Summary of significant accounting policies continued

Commitments and contingencies

Certain conditions may exist as of the balance sheet date, which may result in losses to the Group but the impact of which will only be resolved when one or more future events occur or fail to occur.

If the Group's assessment of contingencies indicates that it is probable that a material loss has been incurred and the amount of the liability can be estimated, then the estimated liability is accrued and charged to the consolidated statement of income. If a probable material loss is within a range and there is no amount within the range which is a better estimate than any other amount, the minimum amount in the range is accrued. If the assessment indicates that a potential material loss is not probable, but is reasonably possible, or is probable but cannot be estimated, than the nature of the contingent liability, together with an estimate of the range of possible loss, is disclosed in the notes to the consolidated financial statements. Loss contingencies considered remote are generally not disclosed unless they involve guarantees, in which case the nature of the guarantee is disclosed.

Recent accounting pronouncements

In December 2010, the FASB issued Accounting Standards Update ('ASU') No. 2010–29, *'Disclosure of Supplementary Pro Forma Information for Business Combinations.'* This ASU requires that the pro forma information be presented as if the business combination occurred at the beginning of the prior annual reporting period for purposes of calculating both the current reporting period and the prior reporting period pro forma financial information. The ASU also requires that this disclosure be accompanied by a narrative description of the amount and nature of material nonrecurring pro forma adjustments. The ASU No. 2010–29 is effective for the Group for the reporting periods ending after December 15, 2010. The Group adopted ASU No. 2010–29 for the 2010 annual financial statements. This adoption did not have a material impact on the Group's results of operations, financial position or cash flows presentation.

In December 2010, the FASB issued ASU No. 2010–28, *'When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts.'* This ASU modifies Step 1 of the goodwill impairment test for reporting units with zero or negative carrying amounts. As a result, ASU No. 2010–28 is eliminating an entity's ability to assert that a reporting unit is not required to perform Step 2 because the carrying amount of the reporting unit is zero or negative despite the existence of qualitative factors that indicate the goodwill is more likely than not impaired. Therefore, goodwill impairments may be reported sooner than under current practice. The ASU No. 2010–28 is effective for the Group for the reporting periods ending after December 15, 2010. The Group adopted ASU No. 2010–28 for the 2010 annual financial statements. This adoption did not have a material impact on the Group's results of operations, financial position or cash flows.

In July 2010, the FASB issued ASU No. 2010–20, *'Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses,'* which amends Accounting Standards Codification ('ASC') No. 310, *'Receivables.'* This ASU provides financial statement users with greater transparency about an entity's allowance for credit losses and the credit quality of its financing receivables and requires entities provide disclosures that facilitate financial statement users' evaluation of the following: 1) the nature of credit risk inherent in the entity's portfolio of financing receivables; 2) how that risk is analysed and assessed in arriving at the allowance for credit losses; 3) the changes and reasons for those changes in the allowance for credit losses. The ASU No. 2010–20 is effective for the Group for the reporting periods ending after December 15, 2010. The Group adopted ASU No. 2010–20 for the 2010 annual financial statements. This adoption did not have a material impact on the Group's results of operations, financial position or cash flows and did not require additional disclosures.

In January 2010, the FASB issued ASU No. 2010–06, *'Improving Disclosures about Fair Value Measurements,'* which requires reporting entities to make new disclosures about recurring or nonrecurring fair-value measurements including significant transfers into and out of Level 1 and Level 2 fair-value measurements and information about purchases, sales, issuances, and settlements on a gross basis in the reconciliation of Level 3 fair-value measurements. This ASU also clarifies existing fair-value measurement disclosure guidance about the level of disaggregation, inputs, and valuation techniques. ASU No. 2010–06 is effective for interim and annual reporting periods beginning after December 15, 2009, except for the detailed Level 3 roll forward disclosures (which are effective for the annual reporting periods starting after December 15, 2010 and for interim periods within those annual reporting periods). The Group adopted the requirements of ASU No. 2010–06 (except for the detailed Level 3 roll forward disclosures) starting from the first quarter of 2010. This adoption did not have a material impact on the Group's results of operations, financial position or cash flows.

Note 3. Cash and cash equivalents

Cash and cash equivalents include the following:

	As of December 31, 2010	As of December 31, 2009
Cash held in banks – US dollars	**357,911**	60,000
Short-term deposits – Russian rubles	**154,730**	212,485
Cash held in banks – Russian rubles	**76,451**	44,110
Short-term deposit – US dollars	**40,033**	115,789
Other	**341**	1,340
Total cash and cash equivalents	**629,466**	433,724

Note 4. Accounts receivable, net

Accounts receivable include the following:

	As of December 31, 2010	As of December 31, 2009
Trade accounts receivable	**243,899**	201,321
Advances given	**8,737**	8,100
	252,636	209,421
Allowance for doubtful accounts	**(17,276)**	(18,367)
Total accounts receivable, net	**235,360**	191,054

Note 5. Inventories

Inventories include the following:

	As of December 31, 2010	As of December 31, 2009
Materials for drilling and workover	**127,918**	110,000
Work in progress	**17,715**	6,801
Total inventories	**145,633**	116,801

Note 6. Property, plant and equipment

Property, plant and equipment include the following:

	As of December 31, 2010	As of December 31, 2009
Machinery and equipment	**964,134**	787,989
Buildings	**38,112**	32,017
Vehicles	**34,712**	25,586
	1,036,958	845,592
Less: accumulated depreciation	**(379,477)**	(251,180)
Construction in progress	**40,146**	73,997
Advances given for property, plant and equipment	**67,557**	15,779
Total property, plant and equipment	**765,184**	684,188

Note 7. Long-term accounts receivable

The Company's long-term accounts receivable were as follows:

	Stated interest rates	**As of December 31, 2010**	As of December 31, 2009
Long-term accounts receivable denominated in US dollars	6.00%	**791**	2,510
Long-term accounts receivable denominated in Russian rubles	0.00%	**6,047**	1,503
Total long-term accounts receivable		**6,838**	4,013

Long-term accounts receivable denominated in US dollars represent amounts receivable from the sale of property, plant and equipment in November 2005 with a carrying value of US $10 million to companies related to a former member of management of the Company. The Group recognised a gain of US $5 million on this transaction. These receivables are secured by a pledge over the assets sold.

Long-term accounts receivable denominated in Russian rubles represent amounts receivable from trade sales during 2009 and 2010 in amount of US $7.0 million and sales of property, plant and equipment as a part of withdrawal of non-core assets program during 2010 in amount of US $10.5 million.

As these interest rates were below market rates at the date of origination these long-term accounts receivable have been recorded on the balance sheet by discounting the initial amount over the period it is to be repaid using market interest rates of 12.24%–15% and 9.91% for Russian ruble and US dollar loans, respectively, estimated by management to be the rate applicable to the Group for borrowings of a similar nature.

Note 8. Restricted cash

The Group had restricted cash of US $61.7 million and US $2.6 million included in other non-current assets as of December 31, 2010 and December 31, 2009, respectively. This amount collateralises the Company's issuance of commercial letters of credit.

The Group had restricted cash of US $6.1 million included in other current assets as of December 31, 2010. This amount consists of a bid bond in the amount of US $1 million and a guarantee issued for a subcontractor in the amount of US $5.1 million.

Note 9. Obligations under capital leases

The Group leases drilling equipment and vehicles under agreements with an option to purchase the leased equipment at the end of the lease term. These assets are accounted for as capital leases.

Included in machinery and equipment and vehicles is US $2.4 million of assets under capital lease as of December 31, 2010 (2009: US $3.6 million).

Property, plant and equipment includes assets under capital lease as follows:

	As of December 31, 2010	As of December 31, 2009
At cost	**3,761**	4,768
Less: accumulated depreciation	**(1,349)**	(1,129)
Net property, plant and equipment	**2,412**	3,639

Future minimum lease payments for the assets under capital lease are as follows:

	As of December 31, 2010
2009	**529**
2010	**529**
2011	**529**
2012	**529**
2013–2018	**1,587**
Total minimum lease payments	**3,703**
Less: amount representing interest	**(1,048)**
Present value of minimum lease payments	**2,655**
Less: current portion (note 10)	**(276)**
Long-term obligations under capital leases (note 11)	**2,379**

Note 10. Current portion of long-term debt

Current portion of long-term debt includes the following:

	As of December 31, 2010	As of December 31, 2009
Current portion of long-term debt (note 11)	**117,274**	31,291
Short-term capital lease obligations (note 9)	**276**	505
Total current portion of long-term debt	**117,550**	31,796

Note 11. Long-term debt

Long-term debt includes the following:

Lender	Final maturity date	As of December 31, 2010	As of December 31, 2009
Debt of the Company			
Loan from stockholders	2011	**70,000**	70,000
Debt of the Company's subsidiaries			
Alfa Bank	2013	**254,291**	–
OAO Sberbank of Russia	2013	**50,275**	58,573
ZAO UniCredit Bank	2012	**11,866**	22,208
Individual	2012	**6,392**	–
Loans from LUKOIL Group companies			
OOO LUKOIL-West Siberia	2011	**7,078**	13,292
OOO LUKOIL-Perm	2041	**1,000**	1,086
OAO Tebukneft	2014	**282**	337
OAO Uhtaneft	2015	**78**	93
OAO LUKOIL	2018	**–**	12,788
OAO LUKOIL Nizhnevolzhskneft	2010	**–**	243
OAO Komineft	2010	**–**	190
OAO LUKOIL-Komi	2010	**–**	2
Total long-term debt		**401,262**	178,812
Current portion of long-term debt (note 10)		**(117,274)**	(31,291)
Long-term capital lease obligation (note 9)		**2,379**	2,858
Total non-current portion of long-term debt		**286,367**	150,379

Stockholders

Long-term loans from stockholders represent loans denominated in US dollars which bear interest at 8.60% and mature on December 31, 2011. These loans were received for the purpose of financing the purchases of property, plant and equipment.

Debt of the Company's subsidiaries

Alfa-Bank

Long-term debt with Alfa-Bank with outstanding balance of US $254.3 million as of December 31, 2010 is denominated in Russian rubles and bears interest at 8.4% per annum.

OAO Sberbank of Russia

Long-term debts with OAO Sberbank of Russia with an outstanding balance of US $50.3 million as of December 31, 2010 are denominated in Russian rubles. These debts were obtained to collateralise the letters of credit opened with OAO Sberbank of Russia related to the acquisition of drilling rigs. Under the terms of debt agreements, these debts bear interest at 3% per annum on unpaid amount of the letters of credit and at LIBOR plus 4.1% per annum on the remaining amount.

ZAO UniCredit Bank

Long-term debt with ZAO UniCredit Bank with outstanding balance of US $11.9 million is denominated in Russian rubles and bears interest at 8.95% per annum.

Notes to consolidated financial statements
continued

(all amounts in thousands of US dollars, unless otherwise noted)

Note 11. Long-term debt continued

Individual

Long-term debt from an individual represents a loan denominated in US dollars which bears interest at 0% and mature on May 1, 2012. This relates to the acquisition of the new workover company OOO Meridian (refer to Note 17). This loan has been recorded at fair value based on the effective interest rate estimated by the management at the acquisition date which was 13% per annum.

This debt is secured by the shares of OOO Meridian.

LUKOIL Group companies

Long-term debt of subsidiaries, denominated in Russian rubles, represents various borrowings from LUKOIL Group Companies. This long-term debt has been recorded at fair value based on effective interest rates estimated by the management at the acquisition date of OOO Burovaya Kompaniya Eurasia, which on average was 12.66%–15% per annum.

Long-term debt is secured by property, plant and equipment with a carrying amount of US $53.2 million as of December 31, 2010 (2009: US $82.3 million).

Maturities of long-term debts outstanding at December 31, 2010 are as follows:

2011	2012	2013	2014	2015	2016 and thereafter	Total
117,274	144,162	138,937	127	31	731	**401,262**

Note 12. Taxes

Income taxes

The Group is taxable in a number of jurisdictions within and outside of the Russian Federation and, as a result, is subject to a variety of taxes as established under the statutory provisions of each jurisdiction.

Operations in the Russian Federation are subject to a Federal income tax rate of 2.0% and a regional income tax rate that varies from 13.5% to 18.0% at the discretion of the individual regional administration.

The Groups' operations outside the Russian Federation are subject to the following rates of income tax:

Kazakhstan	20%
Turkmenistan	20%
Cyprus	10%
Cayman Islands and British Virgin Islands	0%

The majority of the Group's earnings in 2010 and 2009 were taxed in the Russian Federation.

As of December 31, 2010 and 2009, and during 2010 and 2009 the Group did not have any unrecognised tax benefits and thus, no interest and penalties related to unrecognised tax benefits were accrued. The Group's policy is to record interest and penalties related to unrecognised tax benefits as components of income tax expense. In addition, the Group does not expect that the amount of unrecognised tax benefits will change significantly within the next 12 months.

The Company and its subsidiaries file standalone income tax returns in each country in which they operate. Income tax returns are open for inspection by the tax authorities in Russia for tax years 2008–2010, in Turkmenistan for 2009–2010, in Kazakhstan for 2007–2010 and Cyprus for 2005–2010.

There are not currently, and have not been during the two years ended December 31, 2010, any provisions in the taxation legislation of the Russian Federation to permit the Group to reduce taxable profits in a Group company by offsetting tax losses in another Group company against such profits. Tax losses of a Group company in the Russian Federation may, however, be used fully or partially to offset taxable profits in the same company in any of the ten years following the year of loss.

	Year ended December 31, 2010	Year ended December 31, 2009
Current income tax expense	**63,045**	44,896
Deferred income tax expense (benefit)	**8,767**	(1,039)
Total income tax expense	**71,812**	43,857

Note 12. Taxes continued

Income taxes continued

Deferred income taxes are included in the consolidated balance sheets as follows:

	As of December 31, 2010	As of December 31, 2009
Deferred income tax assets – current	**11,407**	11,227
Deferred income tax assets – non-current	**1,422**	277
Deferred income tax liabilities – current	**(478)**	–
Deferred income tax liabilities – non-current	**(24,744)**	(16,009)
Net deferred income tax liability	**(12,393)**	(4,505)

The following table sets out the tax effects of each type of temporary differences which give rise to deferred income tax assets and liabilities:

	As of December 31, 2010	As of December 31, 2009
Accounts payable and accrued liabilities	**5,852**	6,210
Inventories	**4,038**	5,872
Accounts receivable	**2,252**	–
Property, plant and equipment	**1,422**	277
Accrued pension liability	**1,378**	773
Other current assets	**570**	504
Long-term debt	**290**	266
Long-term accounts receivable	**173**	152
Deferred income tax assets	**15,975**	14,054
Property, plant and equipment	**(26,450)**	(17,064)
Accounts receivable	**(917)**	(309)
Other current liabilities	**(854)**	(1,033)
Long-term debt	**(135)**	(136)
Inventories	**(12)**	(17)
Deferred income tax liabilities	**(28,368)**	(18,559)
Net deferred income tax liability	**(12,393)**	(4,505)

Based upon the level of historical taxable income and expectations for future taxable income over future periods, in which the deferred income tax assets are deductible, management believes it is more likely than not the Group will realise the benefits of these deductible temporary differences as of December 31, 2010 and 2009.

The Company has not recognised deferred income taxes on US $654 million of undistributed earnings of its Russian subsidiaries, since such earnings are considered to be reinvested indefinitely. If the earnings were distributed in the form of dividends, the Company would be subject to foreign withholding taxes. The amount of unrecognised deferred income tax liability is US $33 million.

The Company changed its intercompany dividend policy starting July 1, 2010 and will recognise deferred income tax on 20% of the undistributed earnings of its Russian subsidiary OOO Burovaya Kompaniya Eurasia earned beginning January 1, 2011. The earnings of its other Russian subsidiaries as well as the balance of retained earnings of OOO Burovaya Kompaniya Eurasia as of December 31, 2010 are considered to be reinvested indefinitely. Management of the Company has the intention and the ability not to distribute these retained earnings.

Note 12. Taxes continued

Income taxes continued

The following table is a reconciliation of the amount of income tax expense that would result from applying the Russian combined statutory income tax rate to income before income taxes to total income taxes:

	Year ended December 31, 2010	Year ended December 31, 2009
Income before income taxes	**279,165**	209,347
Notional income tax at Russian statutory rate 20%	**55,833**	41,869
Increase (reduction) in income tax due to:		
Non-deductible items, net	**7,461**	1,418
Regional rate differences	**(1,255)**	(1,371)
Withholding tax	**8,103**	–
Foreign rate differences	**1,670**	1,941
Total income tax expense	**71,812**	43,857

Taxes receivable include the following:

	As of December 31, 2010	As of December 31, 2009
Prepaid value added tax	**16,096**	12,977
Prepaid income taxes	**14,169**	18,571
Value added tax recoverable	**3,565**	3,260
Other taxes	**1,130**	964
Total taxes receivable	**34,960**	35,772

Taxes payable include the following:

	As of December 31, 2010	As of December 31, 2009
Value added tax	**32,138**	35,015
Social taxes and contributions	**7,859**	8,267
Personal income tax	**6,559**	5,564
Property tax	**3,139**	2,947
Income taxes payable	**1,942**	326
Road tax	**131**	107
Other taxes	**1,489**	1,237
Total taxes payable	**54,257**	53,463

Note 13. Pension benefits

The Company sponsors a post employment and post retirement benefits program. The primary component of the post employment and postretirement benefits program is a defined benefit pension plan that covers the majority of the Company's employees. This plan is administered by a non-state pension fund, LUKOIL-GARANT, and provides pension benefits. The Company also provides several long-term employee benefits such as death-in-service benefits and lump-sum payments upon retirement of a defined benefit nature.

Additionally the Company provides financial support of a defined benefit nature, to its old age and disabled pensioners who have not vested any pensions under the pension plan. As a result of a decrease in financial support a prior service benefit in the amount of US $1.0 million arose in 2009. It will be amortised starting from 2010 during expected future years of service of participants active at the date of the amendment who are expected to receive benefits under the plan.

Jubilee benefits were calculated for the first time as at December 31, 2010 of US $1.3 million and recognised immediately through the income statement for 2010.

The Company's pension plan primarily consists of a defined benefit plan enabling employees to contribute a portion of their salary to the plan and at retirement to receive a lump sum amount from the Company equal to all past contributions made by the employee up to 3.5% of their annual salary. Employees also have the right to receive upon retirement the benefits accumulated under the previous pension plan when OOO Burovaya Kompaniya Eurasia was a subsidiary of the LUKOIL Group. This plan was replaced in December 2003. These benefits have been fixed and included in the benefit obligation as of December 31, 2010 and 2009. The amount was determined primarily based on a formula including past pensionable service and relative salaries as of December 31, 2003.

Note 13. Pension benefits continued

The Company uses December 31 as the measurement date for its post employment and post retirement benefits program. An independent actuary has assessed the benefit obligations as of December 31, 2010 and 2009.

LUKOIL-GARANT is a multiemployer pension plan in which OOO Burovaya Kompaniya Eurasia and OOO KWWD and OOO UWWD employees participate. The information that follows represents the obligations and assets attributable to OOO Burovaya Kompaniya Eurasia, OOO KWWD and OOO UWWD employees participating in this pension plan.

The following table provides information about the benefit obligations and plan assets as of December 31, 2010 and 2009. The benefit obligations below represent the projected benefit obligation of the pension plan.

	2010	2009
Benefit obligations		
Benefit obligations as of January 1	**11,558**	12,009
Plan amendments	**1,794**	(1,767)
Actuarial gain	**(785)**	(1,095)
Interest cost	**1,037**	997
Service cost	**797**	485
Benefits paid	**(686)**	(654)
Jubilee benefits	**1,268**	–
Effect of exchange rate changes	**(100)**	(348)
Acquisitions	**–**	1,931
Benefit obligations as of December 31	**14,883**	11,558
Plan assets		
Fair value of plan assets as of January 1	**7,770**	7,822
Employer contributions	**515**	320
Other changes in fair value of individual pension accounts	**(230)**	(249)
Return on plan assets	**347**	369
Interest income on individual pension accounts	**304**	304
Benefits paid	**(652)**	(654)
Effect of exchange rate changes	**(60)**	(219)
Fair value of plan assets as of December 31	**7,994**	7,693
Funded status	**(6,889)**	(3,865)
Amounts recognised in the consolidated balance sheet as of December 31, 2010 and 2009		
Accrued pension liability	**(6,889)**	(3,865)

Weighted average assumptions used to determine benefit obligations as of December 31, 2010 and 2009:

	2010	2009
Discount rate	**7.80%**	8.70%
Rate of compensation increase	**7.70%**	8.10%

Weighted average assumptions used to determine net periodic benefit costs for the year ended December 31, 2009 and 2008:

	2010	2009
Discount rate	**8.70%**	9.00%
Expected return on plan assets	**10.07%**	10.89%
Rate of compensation increase	**8.10%**	8.61%

Included in accumulated other comprehensive loss as of December 31, 2010 and 2009, are the following pre-tax amounts that have not yet been recognised in net periodic benefit cost:

	2010	2009
Unamortised prior service (cost) benefit	**(80)**	1,853
Unrecognised actuarial gain	**1,622**	1,050
Total benefit	**1,542**	**2,903**

Note 13. Pension benefits continued

Amounts recognised in other comprehensive loss before tax during the years ended December 31, 2010 and 2009:

	2010	2009
Additional prior service cost (benefit) from plan amendment	1,788	(1,853)
Re-classified prior service benefit amortisation	131	–
Additional gain arising during the period	(593)	(846)
Re-classified gain amortisation	13	–
Net amount recognised in other comprehensive income for the period	1,339	(2,699)

The real expected rates of return on bonds and equities are based on what is observed in the international markets over extended periods of time. In the calculation of the expected return on assets no use is made of the historical returns LUKOIL-GARANT has achieved.

The plans are funded on a discretionary basis through a solidarity account, which is held in trust with LUKOIL-GARANT. LUKOIL-GARANT does not allocate separately identifiable assets to the Group or its other third party clients. All funds of plan assets and other individual pension accounts are managed as a pool of investments.

The asset allocation of the investment portfolio maintained by LUKOIL-GARANT for the Group and its clients was as follows:

Type of assets	As of December 31, 2010	As of December 31, 2009
Bank deposits	41%	42%
Russian corporate bonds	38%	25%
Shares in investment funds	13%	14%
Equity securities of Russian issuers	4%	8%
Russian municipal bonds	2%	4%
Promissory notes of Russian issuers	1%	3%
Shares of OAO 'LUKOIL'	0%	2%
Other assets	1%	2%
	100%	100%

The investment strategy employed by LUKOIL-GARANT includes an overall goal to attain a maximum investment return, while guaranteeing the principal amount invested. The strategy is to invest with a medium-term perspective while maintaining a level of liquidity through proper allocation of investment assets. Investment policies include rules and limitations to avoid concentrations of investments.

The investment portfolio is primarily comprised of two types of Level 1 investments: securities with fixed yield and equity securities. The securities with fixed yield include mainly high yield corporate bonds. Maturities range from one to three years.

Components of net periodic benefit cost were as follows:

	Year ended December 31, 2010	Year ended December 31, 2009
Interest cost	1,037	997
Service cost	797	485
Less expected return on plan assets	(719)	(712)
Amortisation of prior service benefit	(132)	–
Recognised actuarial gain	(13)	–
Jubilee benefits	1,268	–
Total net periodic benefit cost	2,238	770

Total employer contributions for 2010 are expected to be approximately US $0.6 million.

Accumulated benefit obligations were US $10.0 million and US $12.6 million as of December 31, 2010 and December 31, 2009, respectively.

Note 13. Pension benefits continued

The following benefit payments, which reflect expected future services, as appropriate, are expected to be paid:

	2011	2012	2013	2014	2015	5-year period 2011–2015	5-year period 2016–2020
Pension benefits	1,750	692	721	683	814	4,482	2,597
Lump sum payments upon retirement, death and disability	1,736	549	506	460	297	3,699	1,681
Total expected benefits to be paid	**3,486**	**1,241**	**1,227**	**1,143**	**1,111**	**8,181**	**4,278**

Note 14. Fair value of financial instruments

The fair values of all financial instruments are approximately equal to their carrying values as disclosed in the consolidated financial statements. Fair values were determined based on discounted cash flows using estimated market interest rates for similar financial arrangements.

Note 15. Cost of services

Cost of services includes the following:

	Year ended December 31, 2010	Year ended December 31, 2009
Services of subcontractors	**488,950**	320,379
Wages and salaries	**324,924**	222,603
Materials	**218,916**	218,718
Fuel and energy	**79,530**	63,581
Transportation of employees to drilling fields	**23,358**	28,143
Leasing and rent	**10,891**	10,857
Other	**49,322**	47,769
Total cost of services	**1,195,891**	912,050

Note 16. Stockholders' equity

Common and treasury stock

	Year ended December 31, 2010	Year ended December 31, 2009
Authorised and issued common stock, par value 0.01 US dollar each	**146,865,243**	146,865,243
Treasury stock	**(455,797)**	(12,421,825)
Issued and outstanding common stock, par value 0.01 US dollar each	**146,409,446**	134,443,418

During 2010 certain directors of the Group elected to receive GDR's in lieu of cash. 19,854 shares of common stock held as treasury stock were disposed to these directors as a compensation fee.

During 2010 the Group awarded 718,868 shares of common stock held as treasury stock to certain top-managers as a part of its incentive plan (refer to Note 22).

On April 15, 2010 the Company completed the placement of the balance of its GDRs repurchased by the Group as part of its buy-back program at a price of US $19.00 per GDR. One GDR represents one ordinary share.

During 2010 the Group acquired an additional 455,797 shares of common stock for its compensation incentive program.

Dividends and dividends limitations

Profits available for distribution from the Company's Russian subsidiaries to the Company in respect of any reporting period are primarily determined by reference to the statutory financial statements of these subsidiaries prepared in accordance with the laws of the Russian Federation and denominated in Russian rubles. Under Russian Law, dividends are limited to the retained earnings as set out in the statutory financial statements of the Company's Russian subsidiaries. These laws and other legislative acts governing the rights of stockholders to receive dividends are subject to various interpretations.

Retained earnings of the Company's Russian subsidiaries were RUR 19.9 billion and RUR 19.8 billion, respectively as of December 31, 2010 and 2009, pursuant to the statutory financial statements, which at the US dollar exchange rates as of December 31, 2010 and 2009 amount to US $654 million and US $654 million, respectively.

At the Board of Directors meeting on December 14, 2010, dividends were declared for 2010, in the amount of US $0.31 per common stock. Dividends payable by the Company of US $45 million were included in 'Accounts payable and accrued liabilities' in the consolidated balance sheet as of December 31, 2010.

Note 16. Stockholders' equity continued

Dividends and dividends limitations continued

In April 2010 in connection with the placement of its shares held in treasury, the Company announced a one-time special interim dividend of US $179 million. During the reporting period the dividends were fully paid.

At the Board of Directors meeting on December 15, 2009, dividends were declared for 2009, in the amount of US $0.25 per common share. Dividends payable by the Company of US $34 million were included in 'Accounts payable and accrued liabilities' in the consolidated balance sheet as of December 31, 2009.

Earnings per share

The calculation of earnings per share for these years was as follows:

	Year ended December 31, 2010	Year ended December 31, 2009
Net income available for common stockholders	**207,353**	165,490
Weighted average number of outstanding shares	**143,270,265**	135,121,647
Basic earnings per share of common stock (US dollars)	**1.45**	1.22
Contingent shares of stock incentive program (refer to Note 22)	**522,060**	718,868
Weighted average number of outstanding shares, after dilution	**143,792,325**	135,840,515
Diluted earnings per share of common stock (US dollars)	**1.44**	1.22

Note 17. Business combinations

In June 2010, Eurasia Drilling Company Group acquired a 100% interest in OOO Meridian for US $12.2 million which will be paid in three installments ending May 1, 2012. The fair value of consideration comprised US $11.0 million as of the date of acquisition, of which US $4.6 million was repaid in 2010. The remaining amount of US $6.4 million was recognised as a loan payable to the seller (refer to Note 11).

OOO Meridian performs well workover in Komi region. The purpose of the acquisition was to gain access to a new geographical market for workover services allowing more efficient delivery of services.

At the date of acquisition the Group allocated US $9.0 million to goodwill, US $0.7 million to property, plant and equipment, US $2.5 million to current assets, and US $1.2 million to liabilities. The value of property, plant and equipment was determined by an independent appraiser. The main factors that made up the goodwill recognition were related to synergies the Group was expecting to achieve from combined operations. The goodwill is not considered to be deductible for tax purposes.

An impairment loss in amount of US $7.1 million was recognised at December 31, 2010 due to the revision of future development plans. The amount of the loss was determined based on a present value valuation technique.

The revenue and net income of the acquired workover company in amounts of US $8.8 million and US $0.9 million, respectively, included in the Company's consolidated statement of income for the year ended December 31, 2010.

The revenue and net income of the acquired workover company for the whole year ended December 31, 2010 are US $15.9 million (2009: US $9.5 million) and US $1.4 million (2009: US $0.9 million), respectively.

On August 9, 2010 the Group acquired a 100% interest in OOO 'Megionskoye Tamponazhnoye Upravleniye' (OOO MTU) from OOO 'Slavneft-Megionneftegaz' for RUR 275 million (or US $9.0 million at the US dollar exchange rate as of December 31, 2010) paid in cash.

OOO MTU is a Russian provider of cementing services in West Siberia. The purpose of the acquisition was to broaden the spectrum of well construction services, improve the technical efficiency of the Group and to obtain a new customer in West Siberia.

The Group allocated US $7.7 million to property, plant and equipment, US $5.2 million to other assets, US $3.4 million to liabilities and recognised US $0.5 million gain on the bargain purchase. The value of property, plant and equipment was determined by an independent appraiser. The transaction resulted in a gain because the acquired entity was generating low profit margins prior to the acquisition and represented non-core assets of OOO 'Slavneft-Megionneftegaz'.

The revenue and net loss of the acquired company in amounts of US $12.0 million and US $0.1 million, respectively, included in the Company's consolidated statement of income for the year ended December 31, 2010.

The revenue and net income of the acquired company for the whole year ended December 31, 2010 are US $25.3 million (2009: US $22.0 million) and US $0.3 million (2009: US $0.5 million), respectively.

In December 2009, Eurasia Drilling Company Group acquired 100% interests in OOO Tekhgeoservice (OOO TGS) for RUR 1.06 billion (or US $35.0 million at the US dollar exchange rate as of December 31, 2009) paid in cash.

Note 17. Business combinations continued

OOO TGS is a Russian provider of wellsite directional drilling and telemetry services. The purpose of the acquisition was to broaden the spectrum of well construction services and improve the technical efficiency of the Group.

The Group allocated US $30.8 million to goodwill, US $4.6 million to property, plant and equipment, US $3.9 million to current assets, US $0.3 million to long-term deferred tax liabilities and US $4.0 million to other liabilities. The value of property, plant and equipment was determined by an independent appraiser. The main factors that made up the goodwill recognition are related to synergies the Group is expecting to achieve from combined operations, the higher profit margins that the acquired business generates and access to telemetry technology. The goodwill is not considered to be deductible for tax purposes.

In December 2009, Eurasia Drilling Company Group acquired 100% interests in OOO Kogalym Well Workover Division (OOO KWWD) and OOO Urai Well Workover Division (OOO UWWD) for RUR 645 million (or US $21.3 million at the US dollar exchange rate as of December 31, 2009) paid in cash.

OOO KWWD and OOO UWWD perform well workover, well reconditioning and well servicing operations in West Siberia for OAO LUKOIL. The purpose of the acquisition was to increase the Group's market share in workover business.

The Group allocated US $31.1 million to property, plant and equipment, US $28.1 million to other assets, US $13.3 million to short-term and long-term debt, US $0.6 million to long-term deferred tax liability, US $21.2 million to other liabilities and recognised US $2.8 million gain on the bargain purchase. The value of property, plant and equipment was determined by an independent appraiser. The transaction resulted in a net gain because the acquired entities were generating low profit margins prior to the acquisition and represented non-core assets of OAO LUKOIL Group.

Note 18. Commitments and contingencies

Commitments

Commitments for provision of drilling services

In 2009 the Group signed a three-year agreement for drilling services with OAO LUKOIL. Under this agreement the Group will provide drilling services to the LUKOIL Group and precise terms of rendering of such services will be set by signing annual well construction contracts with the LUKOIL Group starting from January 1, 2010 through December 31, 2012. The estimated level of drilling to be performed by the Group during this three-year period was agreed at a minimum of 6.7 million metres. The prices for drilling services under these contracts will be reviewed on an annual basis based on market prices.

The Group estimates that drilling services of at least US $1,139 million will be provided by the Group during 2011.

Insurance

The insurance industry in the Russian Federation and certain other areas where the Group has operations is in the course of development. Management believes that the Group has adequate property damage coverage for its main production assets. In respect of third party liability for property and environmental damage arising from accidents on Group property or relating to Group operations, the Group has insurance coverage that is generally higher than insurance limits set by the local legal requirements. Management believes that the Group has adequate insurance coverage of the risks, which could have a material effect on the Group's operations and financial position.

Litigation

The Group is involved in various claims and legal actions arising in the normal course of business. It is the opinion of management that the ultimate disposition of these matters will not have a material adverse effect on the Group's consolidated financial position, results of operations, or liquidity.

Environmental obligations

Group companies have operated in the Russian Federation, Kazakhstan and Turkmenistan for several years. Environmental regulations are currently under consideration in these countries. Group companies routinely assess and evaluate their obligations in response to new and changing legislation.

As liabilities in respect of the Group's environmental obligations are able to be determined, they are charged against income over the estimated remaining lives of the related assets or recognised immediately depending on their nature. The likelihood and amount of liabilities relating to environmental obligations under proposed or any future legislation cannot be reasonably estimated at present and could become material. Under existing legislation, however, management believes that there are no significant unrecorded liabilities or contingencies, which could have a materially adverse effect on the operating results or financial position of the Group.

Taxation

The taxation systems in the Russian Federation, Kazakhstan and Turkmenistan are relatively new and is characterised by frequent changes in legislation, official pronouncements and court decisions, which are often unclear, contradictory and subject to varying interpretation by different tax authorities. Taxes are subject to review and investigation by a number of authorities, which have the authority to impose severe fines, penalties and interest charges. A tax year remains open for review by the tax authorities during the three subsequent calendar years; however, under certain circumstances a tax year may remain open longer. Recent events within the Russian Federation suggest that the tax authorities are taking a more assertive position in their interpretation and enforcement of tax legislation.

(all amounts in thousands of US dollars, unless otherwise noted)

Note 18. Commitments and contingencies continued

Commitments continued

Taxation continued

The tax authorities in each region may have a different interpretation of similar taxation issues which may result in taxation issues successfully defended by the Group in one region being unsuccessful in another region. There is some direction provided from the central authority based in Moscow on particular taxation issues.

These circumstances may create tax risks that are substantially more significant than in other countries. Management believes that it has provided adequately for tax liabilities based on its interpretations of applicable tax legislations, official pronouncements and court decisions. However, the interpretations of the relevant authorities could differ and the effect on these consolidated financial statements, if the authorities were successful in enforcing their interpretations, could be significant.

Note 19. Related party transactions

In the rapidly developing business environment in the Russian Federation, companies and individuals have frequently used nominees and other forms of intermediary companies in transactions. The senior management of the Company considers that the Group has appropriate procedures in place to identify and properly disclose transactions with related parties in this environment and has disclosed all of the relationships identified which it deemed to be significant.

The Company's General Counsel, Douglas Stinemetz, is a partner with The Stinemetz Law Firm. During 2010 and 2009 the firm billed the Company for costs and expenses of US $2.2 million and US $1.3 million, respectively. Mr. Stinemetz is not otherwise paid for his services as the Company's General Counsel.

In 2007 and 2006, the Company received long-term loans of US $10 million and US $60 million from its stockholders, respectively (refer to note 11). Interest expense of US $6.0 million was recognised and paid during 2010 (2009: US $6.0 million). The outstanding balance was US $70 million as of December 31, 2010 and 2009.

Note 20. Segment information

Presented below is information about the Group's operating and geographical segments for the periods ended December 31, 2010 and 2009, in accordance with ASC 280, *'Disclosures about Segments of an Enterprise and Related Information'*.

The Group has two operating and geographical segments: on-shore drilling conducted in the CIS and off-shore drilling conducted in the Caspian Sea. These segments are based upon the Group's organisational structure, the way in which these operations are managed, the availability of separate financial results, and materiality considerations. Management, on a regular basis, assesses the performance of these operating segments.

Geographical segments have been determined based on the area of operations and include two segments. They are the Caspian Sea and the CIS other than the Caspian Sea.

The transactions between the segments are immaterial. Segment information is summarised as follows:

For the year ended December 31, 2010

	On-shore drilling services (CIS other than the Caspian Sea)	**Off-shore drilling services (Caspian Sea)**	**Consolidated**
Total revenue	**1,699,432**	**112,724**	**1,812,156**
Net income	**179,532**	**27,821**	**207,353**
Total assets	**1,843,745**	**110,323**	**1,954,068**
Goodwill	**32,727**	**–**	**32,727**

For the year ended December 31, 2009

	On-shore drilling services (CIS)	Off-shore drilling services (Caspian Sea)	Consolidated
Total revenue	1,313,068	69,135	1,382,203
Net income	141,782	23,708	165,490
Total assets	1,440,371	83,037	1,523,408
Goodwill	30,792	–	30,792

Note 21. Concentration of credit risk and sales

A significant proportion of the Group's operations are with LUKOIL Group companies and as such the Group has significant concentrations of credit risk with the LUKOIL Group.

Included in the Group's sales and accounts receivables are the following transactions and balances with LUKOIL Group companies.

	2010	2009
Sales for the year ended December 31	**1,290,911**	947,590
Accounts receivable as of December 31	**134,970**	106,500

Note 22. Incentive Compensation Plan

In March 2008, the Company introduced an incentive plan for certain members of management ('participants') for a five year period beginning January 1, 2008. Compensation under this plan is based on a multiple of the participants' annual salary and adjusted for:

- a percentage determined by the increase in the quoted price of the Company's stock from a pre-determined Starting Price to the closing price of the stock in the particular year ('Factor'), and
- the year of compensation under the plan.

The Factor ranges from 0% (where the increase in the stock price is less than 5%) to 100% (where the increase in the stock price is greater than 20%) for any given year during the five year period.

The percentages applied to each of the years under the plan are equal to 12% for 2008, 15% for 2009, 18% for 2010, 25% for 2011 and 30% for 2012.

The Starting Price for the 2008 year was US $27.09 and has been determined with reference to the quoted market price of the Company's shares on the London Stock Exchange ('LSE'). The Starting Price is determined at the beginning of each year based on an average quoted stock price for the last 20 trading days of the preceding year.

The rights to compensation under this plan vest yearly, immediately after the final trading day of the compensation year if the participants are still employed or otherwise in good standing with the Company.

The fair value of the plan was estimated using the Monte Carlo simulation method for the years 2008 to 2012, assuming risk-free interest rates of 0.37% and 1.55% that are based on the yield of one and five year US Treasury securities as of the valuation date, respectively, an expected term of five years and a volatility factor of 48%.

The expected volatility factor was estimated based on the average historical volatility of comparable companies' shares for the previous five year period, ranging from 40% to 86%. The average and median of these were 56% and 48%, respectively. A portion of the award vests upon completion of each plan year and no restrictions apply thereafter. Therefore, no post vesting discount has been applied.

The grant date fair value of the plan was estimated at US $21 million by an independent consulting firm. The Company has approximately US $8.4 million of unrecognised compensation expense as of December 31, 2010 that will be accrued up to December 31, 2012.

The participants may only receive GDRs, each representing one ordinary share of the Company. Therefore, the plan is equity classified. The Group recognised US $4.2 million of compensation expense during 2010. As of December 31, 2010, US $12.6 million is recognised on the Company's balance sheet as an increase in additional paid-in capital.

On February 1, 2010 the Company announced that in accordance with its incentive compensation plan participants of the Plan were awarded 718,868 GDRs for their performance in 2009. One GDR represents one ordinary share.

On February 1, 2011 the Company announced that in accordance with its incentive compensation plan participants of the Plan were awarded 522,060 GDRs for their performance in 2010. One GDR represents one ordinary share.

Note 23. Subsequent events

On February 9, 2011 the Group acquired a 100% interest in Caspian Sea Ventures Limited from Transocean Offshore International Ventures Limited for US $262.0 million paid in cash. Caspian Sea Ventures Limited is the owner of a jack-up drilling rig operating in the Turkmen waters of the Caspian Sea. The purpose of the acquisition was to increase the Company's share in the Caspian offshore drilling market. As of April 19, 2011 the fair value of the assets acquired and liabilities assumed at the acquisition date were not yet determined. Therefore, the initial accounting for the business combination is incomplete.

The Company has evaluated subsequent events from the balance sheet date through April 19, 2011, the date at which the financial statements were available to be issued, and determined there are no other items to disclose.

Corporate information

Directors

Earl of Clanwilliam
Chairman of the Board of Directors
Eurasia Drilling Company Ltd.
Principal, Policy Partnership Ltd.

Alexander Yu. Djaparidze
Chief Executive Officer
Eurasia Drilling Company Ltd.

Richard Matzke
Former Vice-Chairman
of the Board of Chevron

Martin E. Hansen
Former Chief Financial Officer
Eurasia Drilling Company Ltd.

Rene Huck
Former Vice-President, Schlumberger

Victor Kalyuzhny
Former Extraordinary and Plenipotentiary
Ambassador of the Russian Federation
in the Republic of Latvia

Alexander Shokhin
Member, Board of Directors, LUKOIL
Member, Board of Directors, TNK-BP

Officers

Alexander Yu. Djaparidze
Chief Executive Officer

Murat Sampiev
Chief Operating Officer

W. Richard Anderson
Chief Financial Officer

Murray L. Vasilev
Senior Vice President
Business Development

Edward Redd
Senior Vice President Offshore Operations

S. Douglas Stinemetz
General Counsel and Secretary

Kim L. Kruschwitz
Vice President, Marketing and
Investor Relations

Subsidiary officers

Alexander N. Bogachev
President
OOO Burovaya Kompaniya Eurasia

Taleh M. Aleskerov
Senior VP Finance and CFO
OOO Burovaya Kompaniya Eurasia

K. Gagaev
General Director
BKE Shelf Ltd.

Aleksandr N. Kuzev
General Director,
OOO 'SGK-Burenie'
(subsidiary from April 2011)

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CJSC Investment Company
'Troika Dialog'
Credit Suisse Securities (Europe) Limited

Transfer agent

JP Morgan Securities Ltd

Legal advisors

Skadden, Arps, Slate, Meagher &
Flom LLP & Affiliates

Bankers

Barclays Bank PLC
OAO Sberbank (Zapadno-Uralskiy branch)
ZAO Unicredit Bank
OAO Alfa-Bank
ZAO Raiffeisenbank
ZAO VTB Capital

Auditors

ZAO KPMG

Annual General Meeting

The Annual General Meeting
of Members of Eurasia Drilling
Company Limited will be held
on Tuesday, October 25, 2011
in Florence, Italy.

Investor relations contacts

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