CARBON FRIENDLY SOLUTIONS INC.

(A Development Stage Company)

Consolidated Financial Statements

June 30, 2011 and 2010

Tel: 604 688 5421
Fax: 604 688 5132
www.bdo.ca

BDO Canada LLP
600 Cathedral Place
925 West Georgia Street
Vancouver BC V6C 3L2 Canada

INDEPENDENT AUDITOR'S REPORT

To the shareholders of Carbon Friendly Solutions Inc.

We have audited the accompanying consolidated financial statements of Carbon Friendly Solutions Inc., and its subsidiaries which comprise the consolidated balance sheets as at June 30, 2011 and 2010, and the consolidated statements of operations, comprehensive loss and deficit, and cash flows for the years then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Carbon Friendly Solutions Inc. and its subsidiaries as at June 30, 2011 and 2010, and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Emphasis of Matter

Without qualifying our opinion, we draw attention to Note 1 in the financial statements, which indicates that the group has an accumulated deficit of $9,269,414, may incur further losses, and is dependent upon its ability to raise financing to fund operations going forward. These conditions, along with other matters as set forth in Note 1, indicate the existence of a material uncertainty that may cast significant doubt upon the group's ability to continue as a going concern.

BDO Canada LLP

Chartered Accountants

Vancouver, British Columbia
October 28, 2011

CARBON FRIENDLY SOLUTIONS INC.

(A Development Stage Company)
Consolidated Balance Sheets
June 30, 2011 and 2010

	2011	2010
ASSETS		
Current		
Cash and cash equivalents	$ 3,031	$ 156,840
Receivables (note 5)	80,607	113,184
Inventory (note 6)	-	9,567
Prepaid expenses	51,924	22,063
	135,562	301,654
Deposit (Note 8)	56,729	56,729
Property and equipment (note 7)	50,328	31,666
Coal technology and plant prototype (note 4)	8,169,126	-
Intangibles (note 9)	56,287	-
Website development costs (note 10)	21,363	30,519
	$ 8,489,395	$ 420,568
LIABILITIES		
Current		
Accounts payable and accrued liabilities	$ 1,791,642	$ 206,101
Due to related parties (note 13)	440,646	8,630
Loans payable (note 11)	2,503,200	-
	4,735,488	214,731
Future income taxes (note 4)	3,025,474	-
	7,760,962	214,731
SHAREHOLDERS' EQUITY		
Share capital (note 12 (b))	8,650,892	5,321,753
Share subscription receivable (note 12(b))	(352,000)	-
Contributed surplus (note 12 (f))	1,698,955	1,147,344
Deficit	(9,269,414)	(6,263,260)
	728,433	205,837
	$ 8,489,395	$ 420,568

Nature of Operations and Ability to Continue as a Going Concern (note 1)
Commitments (note 17)
Subsequent Events (note 20)

Approved on behalf of the Board:

"Slawomir Smulewicz"
Director

"Stan Lis"
Director

The accompanying notes are an integral part of these consolidated financial statements.

CARBON FRIENDLY SOLUTIONS INC.

(A Development Stage Company)
Consolidated Statements of Operations and Deficit
For the years ended June 30

		2011		2010
Revenues				
Carbon credits	$	7,980	$	45,194
Cost of credits		(9,567)		(79,016)
		(1,587)		(33,822)
Expenses				
Amortization		763,731		23,947
Bank charges and interest		8,445		3,776
Consulting fees (note 13)		581,029		602,676
Finance and sponsorship fees		2,506		-
Interest on notes payable		130,303		-
Investor relations		13,666		61,821
Management fees (note 13)		488,615		449,824
Office and miscellaneous (note 13)		116,670		126,415
Professional fees (note 13)		305,246		199,136
Rent		99,019		195,359
Stock-based compensation (note 12(c)(d))		606,303		402,500
Transfer agent and regulatory fees		10,132		47,830
Travel and promotion (note 13)		207,056		270,347
Wages and benefits		134,214		42,961
Website design		-		25,500
Write down inventory (note 6)		-		6,867
Write down of receivable (note 5)		1,859		23,997
		(3,468,794)		(2,482,956)
Loss before other items and income tax		(3,470,381)		(2,516,778)
Other items				
Interest income		-		1,405
Write down of intangible assets (note 9)		-		(79,621)
Write down (recovery) of property and equipment (note 7)		-		(57,882)
Loss on disposal of subsidiary (note 15)		(2,246)		-
Foreign exchange gain (loss)		105,473		42,447
		103,227		(93,651)
Loss before income tax		(3,367,154)		(2,610,429)
Future income tax recovery		361,000		-
Net loss and comprehensive loss for the year		(3,006,154)		(2,610,429)
Deficit, beginning of year		(6,263,260)		(3,652,831)
Deficit, end of year	$	(9,269,414)	$	(6,263,260)
Loss per share, basic and diluted	$	(0.09)	$	(0.11)
Weighted average number of shares				
Basic and diluted		32,255,034		23,056,446

CARBON FRIENDLY SOLUTIONS INC.
(A Development Stage Company)
Consolidated Statements of Cash Flows
For the years ended June 30

	2011	2010
Cash provided by (used in):		
Operating Activities		
Net loss for the year	$ (3,006,154)	$ (2,610,429)
Items not involving cash:		
Amortization	763,731	23,947
Stock-based compensation	606,303	402,500
Write down of intangible assets	-	79,621
Write down of property and equipment	-	57,882
Write down of inventory	-	6,867
Write down of receivable	1,859	23,997
Future income tax recovery	(361,000)	-
Unrealized foreign exchange	-	(10,786)
Change in non-cash working capital:		
Receivables	30,718	(80,708)
Inventory	9,567	79,017
Prepaid expenses and deposits	(29,861)	(3,983)
Accounts payable and accrued liabilities	742,861	2,928
	(1,241,976)	(2,029,147)
Investing Activities		
Purchase of property and equipment	(957)	(65,859)
Cash acquired on acquisition of MicroCoal	10,036	-
Purchase of intangible assets	(56,287)	(70,972)
	(47,208)	(136,831)
Financing Activities		
Share issuances	1,137,680	-
Share subscriptions	(352,000)	-
Proceeds of loans	22,679	-
Loan repayments	(105,000)	-
Related parties	432,016	
Cash acquired on reverse takeover from common shares issued, net of costs	-	1,831,239
	1,135,375	1,831,239
Effect of foreign exchange	-	2,011
Decrease in cash	(153,809)	(332,728)
Cash, beginning of year	156,840	489,568
Cash, end of year	$ 3,031	$ 156,840
Supplemental cash flow information:		
Interest paid	$ -	$ -
Income taxes paid	$ -	$ -
Non-cash operating, investing and financing activities		
Issuance of shares for acquisition of interest in Microcoal Inc. (note 4)	$ 2,136,767	$ -

1. NATURE OF OPERATIONS AND ABILITY TO CONTINUE AS A GOING CONCERN

The Company was incorporated on April 6, 1990 under the laws of the Province of British Columbia.

The Company is in the business of providing solutions for companies, organizations and individuals looking to reduce or offset their global warming impact caused by greenhouse gas emissions, while including the generation of carbon credits for sale in the global Voluntary and Compliance markets from the completion of reforestation, biomass energy and renewable energy technology projects that are independently validated and verified to globally recognized standards and methodologies. Carbon Friendly Solutions Inc., is also providing coal technology using patented technologies to decontaminate and upgrade low-rank coals for use by power utilities

On October 31, 2007, the Company entered into an agreement with the shareholders of Global CO2 Reduction Inc. ("Global CO2", formerly Carbon Friendly Solutions Inc.) whereby Global CO2 would become a wholly-owned subsidiary of the Company in a reverse takeover transaction. The share exchange closed in September 2008.

These consolidated financial statements include the accounts of the Company since the effective date of the reverse takeover transaction being September 2008 and the historical accounts of the business of Global CO2. Upon closing the acquisition, the Company legally changed its name to Carbon Friendly Solutions Inc.

These consolidated financial statements are prepared on a basis of accounting principles applicable to a going concern, which assumes the realization of assets and satisfaction of liabilities and commitments in the normal course of business. For the year ended June 30, 2011, the Company incurred a loss of $3,006,154 (2010 – $2,610,429) and has an accumulated deficit of $9,269,414 at June 30, 2010 (2010 – $6,263,260) and expects to incur further losses in the development of its business, all of which casts significant doubt about the Company's ability to continue as a going concern. The Company's ability to continue as a going concern is dependent upon its ability to generate future profitable operations and/or to obtain the necessary financing to meet its obligations and repay its liabilities arising from normal business operations when they come due. Management has no formal plan in place to address this concern but is considering obtaining additional funds by equity financing to the extent there is a shortfall from operations. While the Company is expending its best efforts to achieve the above plans, there is no assurance that any such activity will generate funds for operations.

The Company's operations to June 30, 2011 have been financed through debt and the issuance of common shares. If further successful commercialization of the Company's carbon credit business is not achieved, the Company may not have sufficient working capital to sustain operations for the next twelve months.

Although there is no assurance that the Company will be successful in generating future profitable operations, management is confident that the Company will be able to continue as a going concern. Accordingly, these financial statements do not reflect adjustments to the carrying value of assets and liabilities, the reported revenues and expenses and balance sheet classifications used that would be necessary if the going concern assumption were not appropriate. Such adjustments could be material.

Use of estimates

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amount of revenues and expenses during the year. Actual results may differ from these estimates. Significant accounts that require estimates relate to the valuation of coal technology and plant prototype, useful life and impairment of property and equipment and intangible assets, and assumptions used in determining stock-based compensation.

Basis of presentation and consolidation

These consolidated financial statements have been prepared using Canadian generally accepted accounting principles (Canadian GAAP). They include the accounts of the Company and its wholly-owned subsidiaries, Global CO2 Reduction ("Global CO2"), CO2 Reduction Poland Sp. z o.o ("CO2 Reduction"), and its 58.21% owned subsidiary MicroCoal Inc. ("MCI" or "MicroCoal"). All intercompany amounts and transactions have been eliminated on consolidation.

2. SIGNIFICANT ACCOUNTING POLICIES

These consolidated financial statements include the accounts of the Company and the following subsidiaries. All significant intercompany transactions and balances have been eliminated.

	Country of incorporation	Ownership - June 30, 2011	Ownership - June 30, 2010
Global CO2 Reduction Inc.	Canada	100%	100%
CO2 Reduction Poland Sp. z. o. o.	Poland	100%	100%
Pacific Briquetters Inc.	Canada	0%	75%
MicroCoal Inc.	USA	58.21%	0%

2. SIGNIFICANT ACCOUNTING POLICIES continued

Inventory

The Company's inventory is comprised of carbon credit offsets and is stated at lower of cost and net realizable value. Carbon credit offsets are generated through the planting of trees and restoring degraded ecosystems through re-forestation. The planting and re-forestation will generate carbon credits which represent the carbon consumption capability of the planted trees. Directly attributable internally and externally incurred expenditures are allocated on a purchase by purchase basis for each contract and comprises of all production, acquisition and conversion costs. The costs associated with producing inventory are charged to the statement of operations in the same period as the related revenues are recognized. Net realizable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and selling expense.

Carbon credit offsets are recognized in inventory once the methodologies for quantifying, documenting and reporting CO2 removals have been validated and/or verified to International standards by accredited third party validation companies such as Rainforest Alliance or TUV SUD or any of their regional affiliates. The Company follows such recognized standards and methodologies as ISO-14064-2, Climate Community Biodiversity Alliance (CCBA) and the Voluntary Carbon Standard (VCS).

Property and equipment

Property and equipment are recorded at cost. Amortization is recorded using the following rates and methods:

Assets	Rate	Basis
Computer equipment	45%	Declining-balance
Furniture and equipment	20%	Declining-balance
Leasehold improvements	7 years	Straight-line

Intangible assets

Intangible assets that are acquired by the Company or are internally generated are stated at cost less the accumulated amortization and impairment losses.

Costs or cash advances which establish a right to receive carbon credit offsets are classified within intangible assets.

Project costs capitalized are subsequently transferred to inventory in the proportion that validated and verified carbon credit offsets relate to the total expected output from the project. These assets are reviewed annually for impairment. There was an impairment loss in the amount of $79,621 recognized during the year ended June 30, 2010.

Website development costs

Website development costs are recorded at cost and amortized over their estimated useful lives at a rate of 30% declining balance per annum.

Website development costs are written down to their net realizable value if it is determined that their carrying values exceed estimated future benefits to the Company.

It was determined that the website was complete on March 31, 2008. Thereafter, the Company is amortizing deferred website costs at the above rate. For the year ended June 30, 2011, $48,393 (2010 -$39,237) has been amortized.

Impairment of long-lived assets

The Company reviews long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to undiscounted future net cash flows expected to be generated by the asset. When the carrying value exceeds such cash flows, an impairment charge is recognized for the excess. There was an impairment charge in the amount of $65,336 recognized during the year ended June 30, 2010.

Coal technology and plant prototype

In connection with the acquisition of MicroCoal (note 4), the Company acquired patented coal technology and a plant prototype. The technology and the plant prototype were recorded at determined fair value, resulting in a gross asset of $8.91 million and accumulated amortization of $742,648 as of June 30, 2011. The coal technology and plant prototype are being amortized on a straight-line basis over a period of 5 years.

2. SIGNIFICANT ACCOUNTING POLICIES continued

Loss per share

The Company uses the treasury stock method to compute the dilutive effect of options, warrants and similar instruments. Under this method the dilutive effect on loss per share is recognized on the use of the proceeds that could be obtained upon exercise of options, warrants and similar instruments. It assumes that the proceeds would be used to purchase common shares at the average market price during the year. For the years ended June 30, 2011 and 2010, potentially dilutive common shares (relating to options and warrants outstanding at year end) totaling 18,852,070 (2010 – 12,565,200) were not included in the computation of loss per shares because their effect was anti-dilutive.

Basic loss per share is calculated using the weighted-average number of shares outstanding during the year.

Revenue recognition

Revenue is recognized in the period to which it relates and comprises of carbon credit offsets delivered. Revenue is recognized for the sale of carbon credits when the Company has transferred to the buyer the significant risks and rewards of the ownership of the carbon credits, the amount is fixed and determinable and collectability is reasonably assured.

Stock-based compensation

The fair value of all stock-based compensation awards granted is expensed with a corresponding increase to contributed surplus. Compensation expense for employees is generally amortized using the straight-line method over the period from the grant date to the date the options vest. Compensation expense for non-employees is recognized immediately for past services and pro-rata for future services over the service provision period. The fair value of stock-based payments to non-employees is periodically re-measured until the counterparty performance is complete, and any change therein is recognized over the period and in the same manner as if the Company had paid cash instead of paying with or using equity instruments.

Upon exercise of the awards, the related amount of stock based compensation previously expensed is transferred from contributed surplus and together with consideration received, is recorded as share capital.

The Company uses the Black-Scholes option valuation model to calculate the fair value of share purchase options at the date of grant. Option valuation models require the input of highly subjective assumptions, including the expected price volatility. Changes in these assumptions can materially affect the fair value estimate.

Foreign currency translation

The Company's subsidiary activities denominated in currencies other than Canadian dollars are translated as integrated operations using the temporal method. Under this method, monetary items are translated at the exchange rate in effect at the balance sheet date, non-monetary items are translated at historical rates, and revenue and expense items are translated at exchange rates prevailing when such items are recognized in the statement of operations. Exchange gains or losses arising on translation of foreign currency items are included in operating results.

Income taxes

The Company follows the asset and liability method of accounting for income taxes whereby future income taxes are recognized for the future income tax consequences attributable to differences between the financial statement carrying values and their respective income tax bases (temporary differences). Future income tax assets and liabilities arising from a change in tax rates are included in income in the period in which the change occurs. The amount of future income tax assets recognized is limited to the amount that is more likely than not to be realized.

A valuation allowance is recognized to the extent that the recoverability of the future income tax is not considered likely.

Non-controlling interest

Non-controlling interests exist in the less than wholly owned subsidiaries of the Company and represent the outside interest's share of the carrying value of the subsidiaries. (See note 4)

Comparative figures

Certain comparative figures have been reclassified to conform to the current year's presentation.

2. SIGNIFICANT ACCOUNTING POLICIES continued

Financial Instruments

Comprehensive income

The Company adopted CICA Handbook Section 1530, Comprehensive Income. Section 1530 establishes standards for the reporting and presenting of comprehensive income (loss) which is defined as the change in equity from transactions and other events from non-owner sources. Other comprehensive income (loss) refers to items recognized in comprehensive income (loss) ("OCI") that are excluded from net loss. At June 30, 2011 and 2010, the Company had no items that caused other comprehensive loss to be different than net loss.

Financial instruments recognition, measurement, disclosure and presentation

Under Section 3855, all financial instruments are classified into one of five categories: held-for-trading, held-to-maturity investments, loans and receivables, available-for-sale financial assets or other financial liabilities.

All financial instruments and derivatives are measured in the balance sheet at fair value upon initial recognition. Subsequent measurement depends on the initial classification of the instrument. Held-for-trading financial assets are measured at fair value, with changes in fair value recognized in net earnings (loss). Available-for-sale financial instruments are measured at fair value, with changes recorded to OCI until the instrument is measured at amortized costs. All derivative instruments, including embedded derivatives, are recorded in the balance sheet at fair value unless they qualify for the normal sales and purchases exemption. Changes in the fair values of derivatives that are not exempt are recorded in earnings (loss).

The Company has designated its cash and cash equivalents as held-for-trading, its receivables as loans and receivables measured at amortized cost; and its accounts payable and accrued liabilities, loans payable and amounts due to related parties as other liabilities measured at amortized cost. At June 30, 2011, the Company had neither held-to maturity nor available-for-sale financial instruments nor any derivatives or embedded derivatives.

Future changes in accounting policies

Business Combinations, Non-controlling Interest and Consolidated Financial Statements

In January 2009, the CICA issued Handbook Sections 1582 “Business Combinations”, 1601 “Consolidated Financial Statements” and 1602 “Non-controlling Interests” which replace CICA Handbook Sections 1581 “Business Combinations” and 1600 “Consolidated Financial Statements”. Section 1582 establishes standards for the accounting for business combinations that is equivalent to the business combination accounting standard under IFRS. Section 1582 is applicable for the Company’s business combinations with acquisition dates on or after March 1, 2011. Section 1601 together with Section 1602 establishes standards for the preparation of consolidated financial statements. Section 1601 is applicable for the Company’s interim and annual consolidated financial statements for its fiscal year beginning July 1, 2011. Early adoption of these Sections is permitted and all three Sections must be adopted concurrently. Management has not yet determined the financial reporting impact on the adoption of the standards.

International financial reporting standards

In addition to the above new accounting standards, the Accounting Standards Board (“AcSB”), in 2006, published a new strategic plan that will significantly affect financial reporting requirements for Canadian companies. The AcSB strategic plan outlines the convergence of Canadian GAAP with International Financial Reporting Standards (“IFRS”) over an expected five year transitional period. In February 2008, the AcSB announced that 2011 is the changeover date for publicly listed companies to use IFRS, replacing Canada’s own GAAP. The date is for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011. The transition date of July 1, 2011 will require the restatement for comparative purposes of amounts reported by the Company for the year ended June 30, 2011. While the Company has begun assessing the adoption of IFRS for 2011, the financial reporting impact of the transition to IFRS cannot be reasonably estimated at this time.

3. REVERSE TAKEOVER ("RTO") OF GLOBAL CO2 REDUCTION INC.

Pursuant to a Share Exchange Agreement dated October 31, 2007 with the shareholders of Avigo Resources (Avigo), the Company, (legal parent), acquired all of the issued and outstanding shares of Global CO2, (legal subsidiary), in exchange for the issuance of 8 million common shares of the Company. In addition, the Company issued 50,000 common shares as a finder's fee with respect to the acquisition.

Of the 8 million common shares issued in connection with the transaction, 6.05 million are subject to Tier 2 value securities escrow provisions. The escrow provisions contemplate the release of 10 per cent of the escrow shares on the issuance of the TSX-V bulletin and 15 per cent released every six months thereafter, for a total escrow period of 36 months. See note 10(e)

The amounts assigned to the assets and liabilities of the Company are based on the estimated fair value of the net assets of the Company, which equal their carrying values as at September 2, 2008, as follows:

Net assets acquired at assigned value		
Cash	$	1,416,345
Short-term investments		300,000
Receivables		17,459
Advances receivable (i)		325,000
Deferred costs (ii)		311,010
Prepaid expenses		30,000
		2,399,814
Accounts payable and accrued liabilities		(71,873)
Share subscriptions received in advance (iii)		(1,519,680)
Consideration (8,050,000 common shares)	$	808,261

(i) The advance receivable of $325,000 was funds advanced by the legal parent to the legal subsidiary to assist in working capital requirements prior to the reverse takeover transaction. This amount was settled on the completion of the transaction.

(ii) On completion of the transaction, the deferred costs of $311,010 were charged against share capital.

(iii) In conjunction with the reverse takeover, the Company closed a private placement for gross proceeds of $2,072,500 of which $1,519,680 was received by Avigo prior to the close of the private placement and share exchange and is included above in the net assets acquired.

Under reverse takeover accounting, the results of operations of the legal parent have been included in the consolidated financial statements from September 2, 2008.

4. ACQUISITION OF MICROCOAL INC.

The Company entered into an agreement to acquire 58.21% of the outstanding share capital of MCI. In accordance with a share purchase agreement and its amendment, all Microcoal shareholders, except for one, exchanged their shares of Microcoal on a pro rata basis for 10,957,778 common shares of the Company at a price of $ 0.195 per share, as per the Company's share trading price at the January 31, 2011 closing date, which equals a total of $2,136,767 (the "Share Exchange").

At the time of acquisition the fair value of the assets and liabilities of Microcoal were:

Cash	$	10,036
Property and equipment		29,632
Coal technology and plant prototype		8,911,774
Accounts payable and accrued liabilities		(842,680)
Loans payable		(2,585,521)
Future income tax liability		(3,386,474)
Purchase price	$	2,136,767
Consideration paid in shares	$	2,136,767

In addition to the Share Exchange the Company is to complete a private placement financing of up to $6 million (the "Financing") and from such proceeds, the Company is to pay (i) US$1 million cash to a creditor/shareholder of MCI in consideration for the forgiveness of certain outstanding debt owed to such creditor by MCI and for the re-purchase of such creditor's 1,013 MCI shares for cancellation; and (ii) up to US$85,000 cash to certain other creditors of MCI to settle other outstanding indebtedness owed by MCI. Upon completion of the entire transaction, the Company will own 100% of MicroCoal. This transaction did not occur prior to the agreed closing date, September 30, 2011, however, negotiations for the acquisition of the remaining 41.79% interest in MCI is ongoing.

MicroCoal is a materials technology company focused on commercializing the use of microwave energy and related process technologies to transform coal and other minerals into higher quality and higher value industrial materials. The Company accounted for the 58.21% acquisition of MicroCoal as an asset acquisition.

During the year ended June 30, 2011, the Company recorded amortization on the coal technology and plant prototype of $742,648.

5. RECEIVABLES

		2011		2010
GST/HST/VAT recoverable	**$**	**63,266**	$	35,351
Payroll tax receivable		**-**		32,833
Other receivables		**17,341**		45,000
	$	**80,607**	$	113,184

During the year ended June 30, 2011, the Company determined that the collectability of a portion of its VAT receivable was unlikely and recorded an impairment charge of $1,859 in the consolidated statement of operations (2010 - $23,997).

6. INVENTORY

		2011		2010
	$	-	$	9,567

During the year ended June 30, 2010, the Company wrote-down the value of inventory to its net realizable value and recorded an impairment charge of $6,867 in the consolidated statement of operations.

7. PROPERTY AND EQUIPMENT

				June 30, 2011				June 30, 2010
		Cost		**Accumulated amortization**		**Net book value**		Net book value
Computer equipment	$	34,861	$	23,326	**$**	**11,535**	$	13,475
Furniture and equipment		74,466		40,595		**33,871**		12,038
Leasehold improvements		8,614		3,692		**4,922**		6,153
Total	$	117,941	$	67,613	**$**	**50,328**	$	31,666

During the year ended June 30, 2010, the Company recorded a $57,882 impairment charge in the consolidated statement of operations.

8. DEPOSIT

The deposit represents an amount paid in advance for the lease of office premises.

9. INTANGIBLE ASSETS

		2011		2010
Exclusive sales contract (i)	**$**	**111,408**	$	55,121
Rights to wood waste and recycling permit (ii)		**-**		24,500
Impairment charge (i) and (ii)		**(55,121)**		(79,621)
	$	**56,287**	$	-

(i) Exclusive Sales Contract

During the year ended June 30, 2011 and 2010, the Company entered into additional sales contracts for the exclusive rights to sell carbon credits generated from the bedding and trees growing on plots of land located in Poland. Additional lease payments are conditional on the earlier of the date of certification of validation carbon credits or sale of a carbon credit units generated from the plots of land.

As of June 30, 2011, the Company reviewed the carrying amount of its intangible assets and recognized an impairment charge of $nil in the consolidated statement of operations. (June 30, 2010 - $55,121)

(ii) Rights to Wood Waste and Recycling Permit

Pursuant to the agreements with 0733403 B.C. Ltd. ("TCG") the Company paid $24,500 to TCG in connection with the PBI venture arrangement (note 15). On October 6, 2010, the Company terminated this agreement and arrangement with TCG (note 15).

As of June 30, 2011, the Company reviewed the carrying amount of its intangible assets and recognized an impairment charge of $nil in the consolidated statement of operations. (June 30, 2010 - $24,500)

10. WEBSITE DEVELOPMENT COSTS

	June 30, 2011			June 30, 2010
	Cost	**Accumulated amortization**	**Net book value**	Net book value
Website development costs	$ 69,756	$ 48,393	$ 21,363	$ 30,519

11. LOANS PAYABLE

	2011	2010
Pursuant to several loan agreements, a total of $385,000 was advanced to the Company on an unsecured basis. A 20% loan bonus was charged with the loan amount calculated at $462,000 to be repaid. The interest rate is 8% per annum and the term is one year or shorter if a financing was achieved by the Company. During the year ended June 30, 2011 the Company repaid $202,000 with the principal balance owing at June 30, 2011 being $260,000. The due dates range from October 2011 to January 2012. The 20% loan bonus is included in prepaid expense and amortized to interest expense over the term of the loan.	$ 260,000	$ -
Pursuant to a loan agreement a total of $20,000 was advanced to the Company on an unsecured basis. The interest rate is at 2% per month. The due date is March 17, 2012 unless a financing was achieved by the Company.	20,000	-
Pursuant to a loan agreement a total of $20,000 was advanced to the Company on an unsecured basis. The interest rate is at 2% per month. The loan is payable on demand.	20,000	-
Pursuant to a loan agreement dated June 2, 2008, MicroCoal received $2,250,000 USD, on an unsecured basis, in periodic payments at a rate of interest at 6.75% per annum. The loan was payable on demand however, as a result of the acquisition agreement where the Company acquired a 58.12% interest in MicroCoal (note 4), there was a provision to limit the liabilities to MicroCoal for a total of $1,000,000 USD if the Company was to continue to acquire the balance of shares in MicroCoal and provide financing.	2,203,200	-
	$ 2,503,200	$ -

12. SHARE CAPITAL

(a) Authorized: 100,000,000 common shares without par value

(b) Issued and Outstanding	**Shares**	**Amount**	**Share subscriptions**
Balance, June 30, 2009	19,913,927	$ 3,498,850	$ -
Stock options exercised	297,500	74,175	-
Private placement	7,347,000	1,983,690	-
Share issuance costs	-	(226,626)	-
Fair value of agent's warrants	-	(65,191)	-
Fair value of stock options exercised	-	56,855	-
Balance, June 30, 2010	27,558,427	5,321,753	-
Private placement	5,272,750	1,052,830	-
Share subscriptions	-	-	(352,000)
Stock options exercised (note 12(d))	395,000	84,850	-
Shares issued for acquisition of MicroCoal (note 4)	10,957,778	2,136,767	-
Fair value of stock options exercised	-	54,692	-
Balance, June 30, 2011	44,183,955	$ 8,650,892	$ (352,000)

Fiscal 2011

During the year ended June 30, 2011, a private placement was completed consisting of 5,272,750 units at $0.20 per unit, each unit consisting of one common share and one share purchase warrant to purchase one common share at $0.35 per share for a period of two years. Issue costs of $1,720 were incurred. As at June 30, 2011 $352,000 remain as share subscriptions receivable, but were collected subsequent to year end (note 20).

All proceeds from the above private placements were allocated to share capital with no amounts allocated to the attached warrants.

Fiscal 2010

During the year ended June 30, 2011, a private placement was completed consisting of 7,347,000 units at $0.27 per unit, each unit consisting of one common share and one share purchase warrant to purchase one common share at $0.35 per share for a period of two years. The private placement was completed in three tranches consisting of 1,882,000, 1,400,000 and 4,065,000 respectively from November 20, 2009 to December 11, 2009 . In connection with the private placement 328,200 share purchase warrants were issued as finder fees' ("agent warrants") exercisable at a price of $0.35 per share for a period of two years. The fair value of the agent warrants was $65,191 using the Black Scholes Option Pricing Model assuming no dividends are to be paid, with a weighted average expected life of 2 years, a weighted average volatility of 110% and an average annual risk free interest rate of 0.5%. The Company paid share issuance costs of $226,626 related to legal fees, transfer fees and finders' fees.

All proceeds from the above private placements were allocated to share capital with no amounts allocated to the attached warrants.

12. SHARE CAPITAL continued

c) Warrants

A summary of the status of the warrants outstanding is as follows:

	Number of shares	Exercise Price
Balance, June 30, 2009	2,072,500	$ 0.75
Issued	7,675,200	0.35
Balance, June 30, 2010	9,747,700	0.44
Issued	5,272,750	0.35
Balance, June 30, 2011	15,020,450	$ 0.41

The following table summarizes warrants outstanding and exercisable at June 30, 2011:

Warrants Outstanding	Warrants Exercisable	Exercise Price	Expiry Date
2,072,500 *	2,072,500	$0.75	August 29, 2012
2,070,200	2,070,200	$0.35	November 30, 2011
1,540,000	1,540,000	$0.35	December 3, 2011
4,065,000	4,065,000	$0.35	December 11, 2011
5,272,750	5,272,750	$0.35	June 30, 2013
15,020,450	15,020,450		

* 2,072,500 warrants with an original expiry date of August 29, 2010 were extended to August 29, 2012. Stock-based compensation related to the warrant extension has been recorded in the amount of $294,938, which was calculated using the Black-Scholes option pricing model using a risk free interest rate of 2.87%, an expected dividend yield of $nil, a stock price volatility of 124% and an expected life of warrants of 2.03 years.

d) Stock options

On December 29, 2010, the Company adopted an incentive share option plan for granting options to directors, employees and consultants, under which the total outstanding options are limited to 10% of the issued and outstanding common shares of the Company. The options vest when granted except for options granted for investor relations activities which vest over a 12 month period with no more than 25% of the options vesting in any three month period.

Stock options outstanding are as follows:

	Number of shares	Weighted Average Exercise Price
Outstanding, June 30, 2009	1,965,000	$ 0.24
Granted	1,150,000	0.36
Exercised	(297,500)	0.25
Outstanding, June 30, 2010	2,817,500	0.29
Granted	2,321,620	0.20
Cancelled	(912,500)	0.29
Exercised	(195,000)	0.23
Exercised	(200,000)	0.20
Outstanding, June 30, 2011	3,831,620	$ 0.24

During the year ended June 30, 2011, the Company granted 2,321,620 options to employees, directors and consultants. The options vested immediately, have an exercise price of $0.20 and expire on February 8, 2016.

12. SHARE CAPITAL continued

The following table summarizes stock options outstanding and exercisable at June 30, 2011:

Options Outstanding	Exercise Price	Expiry Date	Options Exercisable
75,000	$0.27	April 20, 2012	75,000
905,000	$0.23	October 6, 2013	905,000
30,000	$0.23	March 14, 2014	30,000
700,000	$0.36	December 16, 2014	700,000
2,121,620	$0.20	February 8, 2016	2,121,620
3,831,620			3,831,620

During the year ended June 30, 2011, stock-based compensation has been recorded in the amount of $311,365 (2010 - $402,500) and included in contributed surplus. The weighted average life of the options is 3.76 years.

The compensation costs recorded in the consolidated statements of operations and deficit were calculated using the Black-Scholes option pricing model using the following weighted average assumptions:

	2011	2010
Risk free interest rate	**2.78%**	2.90%
Expected dividend yield	**nil%**	nil%
Stock price volatility	**83.0%**	88.0%
Expected life of options	**4.70 years**	4.68 years

The weighted average fair value of options granted during the year ended June 30, 2011 is $0.13 (2010 – $0.32).

e) Escrow shares

Pursuant to the reverse takeover transaction (note 3), 6.05 million common shares are subject to Tier 2 value securities escrow provisions. The escrow provisions contemplate the release of 10 per cent of the escrow shares on the issuance of the TSX-V bulletin and 15 per cent released every six months thereafter, for a total escrow period of 36 months.

As at June 30, 2011, 907,500 (June 30, 2010 – 2,722,500) common shares remain in escrow. 1,815,000 common shares were released from escrow during the year ended June 30, 2011 (2010 - 1,815,000).

f) Contributed Surplus

	2011	2010
Balance, beginning of year	$ 1,147,344	$ 736,508
Stock-based compensation	311,365	402,500
Fair value of agent warrants (note 12(c))	294,938	65,191
Fair value of stock options exercised, reclassified to share capital (note 12(b))	(54,692)	(56,855)
Balance, end of year	$ 1,698,955	$ 1,147,344

13. RELATED PARTIES

The following expenses were incurred with directors and officers of the Company

	For the year ended June 30, 2011	For the year ended June 30, 2010
Management and directors' fees	**$ 488,615**	$ 449,824
Consulting	**44,417**	131,200
Automobile allowance (travel and promotion)	**28,808**	43,200
Rent	**-**	78,342
Professional fees	**69,500**	29,900
Office and miscellaneous	**1,882**	7,500
Total	**$ 633,222**	$ 739,966

As at June 30, 2011 $440,646 (June 30, 2010 - $8,630) was owing to officers and directors. The amounts due are unsecured, non-interest bearing and have no fixed terms of repayment.

The amounts charged to the Company for the services provided have been determined by negotiation among the parties and in certain cases, by signed agreements. These transactions were measured at the exchange amount which is the amount of consideration established and agreed to by the related parties.

14. INCOME TAXES

A reconciliation of income taxes at statutory rates with the reported taxes follows:

	2011	2010
Statutory rates in Canada	**27.50%**	29.25%
Income taxes at Canadian statutory rates	**$ (926,000)**	$ (763,500)
Difference in tax rates in other jurisdictions	**(102,000)**	73,000
Change in statutory rate	**40,000**	81,100
Tax effect of disposal of subsidiaries	**46,000**	
Share issue costs	**-**	(56,700)
Permanent differences	**222,000**	132,400
	(720,000)	(533,700)
Increase in valuation allowance	**359,000**	533,700
Future income tax expense/(recovery)	**$ (361,000)**	$ -

Future income tax asset (liability)	25%	25%
Tax losses carried forward	**$ 1,573,000**	$ 1,091,000
Undeducted financing costs	**80,000**	113,000
Capital assets	**9,000**	-
Other tax assets	**-**	34,000
Coal technology and plant prototype	**(3,090,000)**	-
	(1,428,000)	1,238,000
Valuation allowance	**(1,597,000)**	(1,238,000)
Net future income tax asset (liability)	**$ (3,025,000)**	$ -

As at June 30, 2011, the Company has non-capital losses of approximately $5.933 million to reduce future taxable income and which expire during the years 2027 to 2031. For Polish tax purposes, there are approximately $844,000 of non-capital losses which have not been recognized due to the uncertainty of the recognition of these losses. The company evaluates its valuation allowance requirements based on projected future operations. When circumstances change and this causes a change in management's judgment about the recoverability of deferred tax assets, the impact of the change on the valuation allowance is reflected in current income. In 2011 and 2010, a valuation allowance was applied to all net future tax assets.

15. PACIFIC BRIQUETTERS INC. ("PBI")

During the year ended June 30, 2010, the Company incorporated Pacific Briquetters Inc. ("PBI"), a British Columbia company, for the purpose of owning, financing, developing, constructing and operating a proposed briquette and bio energy manufacturing and distribution facility and business to be operated on certain lands and premises located in Mission, BC (the "Premises"), which were owned and operated by Green River Log Sales Ltd., an affiliate of TCG and a company unrelated to Carbon Friendly Solutions Inc., which, in consideration thereof, was a 25% shareholder, with the Company owning 75%, in PBI going forward (collectively, the "Venture"). During 2011 the Company decided not to proceed with this business and divested itself of any interest.

Pursuant to an agreement that provides in consideration of TCG agreeing to provide for the benefit of PBI and during the continuance of the Venture;

(i) all of TCG's existing rights and entitlement to a proposed wood waste and recycling permit to be provided in respect of the Premises;

(ii) a 20-year renewable, at the option of PBI, commercial lease agreement respecting the Premises; and

(iii) certain consulting services under a consulting services agreement providing for both the staffing and operation of the Venture on the Premises.

(iv) subject to the following performance vesting criteria (the "Vesting Criteria") during the Venture, the issuance to TCG by the Company of an aggregate of 2,000,000 vesting and non-transferable common stock share purchase warrants (each a "Warrant") to acquire an equivalent number of common shares of the Company (each a "Warrant Share"), at an exercise price of $0.40 per Warrant Share, and exercisable for a period of three years from the date of issuance of the Warrants (the "Warrant Exercise Term"). Each of the subject Warrants will vest and only become exercisable by TCG during the Warrant Exercise Term in the following manner and in the following denominations upon the attainment of the following Vesting Criteria:

(a) an aggregate of an initial 500,000 of the Warrants will become immediately exercisable by TCG upon the attainment by PBI during the Warrant Exercise Term of an aggregate of not less than $500,000 in gross profits (the "Gross Profits" – defined as total revenues during that period less the costs of all products sold by the Company in connection with said revenues);

(b) an aggregate of a further 500,000 of the Warrants will become immediately exercisable by TCG upon the attainment by PBI during the Warrant Exercise Term of an aggregate of not less than $1,000,000 in Gross Profits;

(c) an aggregate of a further 500,000 of the Warrants will become immediately exercisable by TCG upon the attainment by PBI during the Warrant Exercise Term of an aggregate of not less than $1,500,000 in Gross Profits; and

(d) an aggregate of the final 500,000 of the Warrants will become immediately exercisable by TCG upon the attainment by PBI during the Warrant Exercise Term of an aggregate of not less than $2,000,000 in Gross Profits.

During the year ended June 30, 2010, the Company has paid the sum of $100,000 towards start up costs of PBI and paid $24,500 (note 9) on initiation of the agreement to TCG.

15. PACIFIC BRIQUITTERS INC. ("PBI") continued

The Company had determined as of June 30, 2010 that the performance vesting criteria has not been met as no gross profits from the venture have occurred or is reasonably expected to occur and therefore, has not issued to TCG measured or recognized the common share purchase warrants in these financial statements.

Non-controlling interest

The fair value of the non-controlling interest in PBI was determined based on the proportionate share (25%) of the underlying assets and liabilities of PBI. There were no net identifiable assets acquired in the formation of the arrangement between TCG and the Company.

Upon consolidation, losses of PBI cannot be allocated to non-controlling interests in excess of its carrying value in PBI. Consequently, all of PBI's losses have been allocated to the Company during the year ended June 30, 2010.

16. SEGMENTED INFORMATION

The Company currently operates in one industry segment, being the generation of carbon credits and in the geographic areas as follows.

		2011		2010
Sales for the year				
Canada	$	-	$	45,194
USA		-		-
Poland		7,980		-
	$	7,980	$	45,194
Property and Equipment				
Canada	$	21,920	$	29,638
USA		27,120		-
Poland		1,288		2,028
	$	50,328	$	31,666
Intangible Assets				
Canada	$	-	$	-
USA		-		-
Poland		56,287		-
	$	56,287	$	-
Coal technology and plant prototype				
Canada	$	-	$	-
USA		8,169,126		-
Poland		-		-
	$	8,169,126	$	-

17. COMMITMENTS

(a) The Company has one consulting agreements for a period of 3 years commencing July 1, 2010 for $120,000 per year, respectively. There is an annual increase of 5% per annum. In an event of a change in control, and the officer is terminated within 12 months of such change of control, then the officer will receive a lump sum payment equal to the greater of (1) the compensation remaining for the rest of the period under the terms of engagement and (2) one year’s compensation.

(b) The Company entered into an agreement to lease additional office space for five years as follows:

2012	$	94,923
2013		94,923
2014		96,714
2015		98,505
	$	385,065

(c) The Company has acquired to rights to over 100 properties wherein it has the exclusive sale contract rights to sell carbon credits generated from the bedding and trees growing in various plots of lands in Poland until 2040. The Company paid a total of $111,408 for these exclusive sales contract rights and is obligated to pay 8,177,216 PLN (approximately $2.9 million) within 30 days subject to obtaining carbon credit certification or sale of a carbon credit unit from the lands. The rights expire starting from November 2011 to December 2012.

18. CAPITAL DISCLOSURES

The Company manages its capital structure and makes adjustments based on the funds available in order to support continued operation and future business opportunities. The board of directors does not establish quantitative return on capital criteria for management, but rather relies on the expertise of the Company's management to sustain future development of the business. The Company considers its capital to be share capital. The capital management objectives remain the same as for the previous fiscal period.

The Company’s operations are currently not generating positive cash flow; as such, the Company is dependent on external financing to fund its activities. In order to carry out potential expansion and to continue operations, and pay for administrative costs, the Company will spend its existing working capital, and raise additional amounts as needed. Companies in this stage typically rely upon equity and debt financing or joint venture partnerships to fund its operations. There is no certainty with respect to the Company’s ability to raise capital.

Management reviews its capital management approach on an ongoing basis and believes that this approach, given the relative size of the Company, is reasonable. As at June 30, 2011, cash amounted to $3,031. During the twelve month period ended June 30, 2011, the Company raised $1.14 million through the issuance of common shares in a private placement and on exercise of stock options. These additional funds were used for the acquisition of property and equipment and intangible assets and for working capital requirements.

The Company is not exposed to external requirements by regulatory agencies regarding its capital.

19. FINANCIAL INSTRUMENTS AND RISKS

As at June 30, 2011, the Company's financial instruments consist of cash, receivables, accounts payable and accrued liabilities and loans payable. The fair values of these financial instruments approximate their carrying values because of their current nature or adjustments to fair value made at each period end.

Fair Value

The Company classifies its fair value measurements in accordance with an established hierarchy that prioritizes the inputs in valuation techniques used to measure fair value as follows:

Level 1 - Unadjusted quoted prices in active markets for identical assets or liabilities

Level 2 - Inputs other than quoted prices that are observable for the asset or liability either directly or indirectly, and

Level 3 - Inputs that are not based on observable market date

The following table sets forth the Company's financial assets measured at fair value by level within the fair value hierarchy:

	Level 1	Level 2	Level 3	2011
Cash	$ 3,031	$ -	$ -	$ 3,031

	Level 1	Level 2	Level 3	2010
Cash	$ 156,840	$ -	$ -	$ 156,840

Market Risk

Market risk is the risk of loss that may arise from changes in market factors such as interest rates, investment fluctuations, and commodity and equity prices. Market conditions will cause fluctuations in the fair values of financial assets classified as held-for-trading and available-for-sale and cause fluctuations in the fair value of future cash flows for assets or liabilities classified as held-to-maturity, loans or receivables and other financial liabilities. The Company is not exposed to significant market risk. The Company is not exposed to significant interest rate risk as the Company has no variable interest debt. The Company's ability to raise capital to fund activities is subject to risks associated with fluctuations in the carbon market. Management closely monitors individual equity movements and the stock market to determine the appropriate course of action to be taken by the Company.

19. FINANCIAL INSTRUMENTS AND RISKS - Continued

Liquidity Risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. The Company manages liquidity risk through the management of its capital structure and financial leverage as outlined in note 18.

Interest rate Risk

The Company is not exposed to significant interest rate risk due to the short-term maturity of its monetary assets and liabilities and amounts owing being non-interest bearing or bearing fixed rates of interest.

Credit Risk

The Company is not exposed to significant credit risk on its financial assets due to cash being placed with major financial institutions and GST/HST recoverable is due from government agencies.

Currency Risk

The Company is exposed to foreign currency risk on fluctuations related to cash, receivables and accounts payable and accrued liabilities that are denominated Polish Zloty (PLN) and the United States dollar (USD). Management does not hedge its exposure to foreign exchange risk and does not believe the Company's net exposure to foreign currency risk is significant.

The following table provides an indication of the Company's significant foreign exchange currency exposure as at June 30, 2011:

	United States		Poland	
	2011	2010	2011	2010
Cash	1,987	-	312	10,402
Accounts and loans payable	(3,613,911)	-	(90,548)	(44,249)
	(3,611,924)	-	(90,236)	(33,847)

The following exchange rates applied during the year ended June 30, 2011:

	Average rate	Spot rate
Canadian dollars to US dollars	0.9987	1.0212
Canadian dollars to Zloty	2.9058	2.8254

Based on the Company's foreign currency exposures noted above, varying the above foreign exchange rates reflecting a 1% strengthening of the Canadian dollar to Zloty would have respectively decreased the net loss by $2,558 and a 1% strengthening of the Canadian dollar to US dollar would have respectively decreased the net loss by $36,905.

v) Other Price and Market Risk

The Company's financial instruments are all short term and exposed to other price and market risks should the fair value of future cash flows from financial instruments fluctuate.

The carbon market is a newly developing market and as such there are limited avenues to negate market risk in traditional manners. The Company monitors and understands movements within the market on a regular basis.

20. SUBSEQUENT EVENTS

Stock Options

The Company granted 790,000 stock options to two directors and one officer. The options vested immediately, have an exercise price of $0.14 and expire on August 16, 2016.

Share Purchase Agreement

The Company executed a share purchase agreement with the shareholders of Carbiopel - Eco Stream Power S.A. ("Carbiopel") pursuant to which the Company will acquire 51% of the issued and outstanding shares of Carbiopel, set out in the amendment to the share purchase agreement (the "Amended Agreement") between the Company and the Carbiopel shareholders dated July 14, 2011. The terms of the agreement provide the Company can purchase 1% of Carbiopel by the issuance of 400,000 shares of the Company and 50% of Carbiopel for cash payments of $400,000.

Pursuant to terms of the Amendment Agreement the Company purchased 2,000 of the issued and outstanding shares of Carbiopel from the Carbiopel shareholders, representing 1% of Carbiopel, for the issuance of 400,000 common shares in the capital of the Company (trading price on the day the shares were issued was $0.27 per share).

Share subscriptions

The Company received share subscriptions of $352,000 subsequent to June 30, 2011.

Private placement

The Company is in the process of closing a non-brokered private placement that was previously announced on June 21, 2011 (“Offering”). The Company intends to raise total financing of $2,153,550 in gross proceeds from the subscription of 10,767,750 Units and has raised $1,090,000 to date in cash and other consideration. Each Unit consists of one common share and one common share purchase warrant (the “Warrant”). Each Warrant entitles the holder thereof to purchase one common share of the Company (one “Common Share”) at an exercise price of $0.35 per Common Share for a period of two years from the closing date of the Offering.