

CARBON FRIENDLY SOLUTIONS INC.

MANAGEMENT DISCUSSION AND ANALYSIS

September 30, 2011

1.1 Forward Looking Information

This Management Discussion and Analysis ("MD&A") of Carbon Friendly Solutions Inc. ("Carbon Friendly" or the "Company") has been prepared by management as of December 27, 2011 and should be read in conjunction with the unaudited condensed interim consolidated financial statements and related notes thereto of the Company for the three months ended September 30, 2011, which were prepared in accordance with Canadian generally accepted accounting principles.

The following discussion contains, in addition to historical information, forward-looking statements that involve risks and uncertainties. These forward-looking statements may include, among other things, statements concerning plans, objectives and future economic prospect, expectations, beliefs, future plans and strategies, anticipated events or trends and similar expressions concerning matters that are not historical facts. These forward-looking statements involve known and unknown risks, uncertainties and other factors which may cause actual results, performance or achievements and industry result, to be materially different from what is said or implied with such forward-looking statements.

Some of the factors that could cause results or events to differ from current expectations include, but are not limited to, the factors described under "Risk Factors". The financial statements of Carbon Friendly are presented in Canadian dollars and in accordance with generally accepted accounting principles in Canada.

1.2 Over-all Performance

Company Overview

The Company was incorporated on April 6, 1990 under the laws of British Columbia. On August 18, 2000 the Company changed its name from Anthian Resources Corp. to Sudamet Ventures Inc. On May 4, 2005, the Company changed its name again from Sudamet Ventures Inc. to Avigo Resources Corp.

On September 2, 2008, the Company completed a share exchange with Global CO2 Reduction Inc. (Global CO2) and changed its name to Carbon Friendly Solutions Inc. The Company is listed on the TSX Venture Exchange under the symbol "CFQ" and the Frankfurt Stock Exchange under the symbol "0FS-FRA" ("zero FS-FRA").

On December 31, 2010, the common shares of the Company became listed for trading on the Canadian National Stock Exchange ("CNSX") under the symbol of "CFQ". The Company applied to the TSX Venture Exchange ("TSX-V") to delist its shares from the TSX-V, and received confirmation that effective at the close of business on December 31, 2010 the Company's share will be delisted from the TSX-V.

The Company was founded as a project proponent that provides 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 and finding economic solutions for the reduction of carbon footprints in power generation.

Global CO2 Reduction Inc. and CO2 Reduction Poland Sp. z o.o.

Through its wholly owned subsidiaries, Global CO2 Reduction Inc. and CO2 Reduction Poland Sp. z o.o., Carbon Friendly is focusing on removing and offsetting carbon dioxide emissions from the completion of reforestation, biomass energy and renewable energy technology projects that are independently validated and verified to globally recognized standards and methodologies.

CO2 Reduction Poland mainly acts as an aggregator and cultivator of lands, thus collecting together areas that are fragmented among many small owners and coordinating the planting of trees to complete forestation programs.

Carbon Friendly is focusing on reducing carbon emissions through carbon sequestration projects in Europe and surrounding areas, by planting trees called afforestation or reforestation. Poland and neighbouring countries hold vast potential for land-use, land-use change and forestry (LULUCF) projects that qualify under Kyoto and post-Kyoto mechanisms as well as non-Kyoto schemes. As a result, inactive or converted vacant land, including pasture or post-agricultural land is leased to Carbon Friendly from land owners, usually for a period of 20 to 30 years.

Typically these areas are forested with an accepted and approved assortment of fast growing tree species to maximize carbon absorption in that region. The carbon sequestration occurs naturally through photosynthesis, which is the process of using energy in sunlight to convert water and carbon dioxide into carbohydrates and oxygen.

MicroCoal, Inc. ("MicroCoal")

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. Our initial target market is the coal-fired segment of the North American electrical utility industry. Coal-fired power plants currently produce nearly 50% of the electricity in the U.S.A. MicroCoal's proprietary on-site process cleans up coal at the power plant prior to combustion by reducing contaminants like sulfur and mercury and also improving fuel efficiency by removing water. This is helping to accelerate the existing trend of fuel switching to low-rank Powder River Basin (western) coals. We are building on our extensive portfolio of patents pending and proprietary know-how and see significant growth potential into new geographies and new industrial markets.

Summary of Activity to Date

Forestry

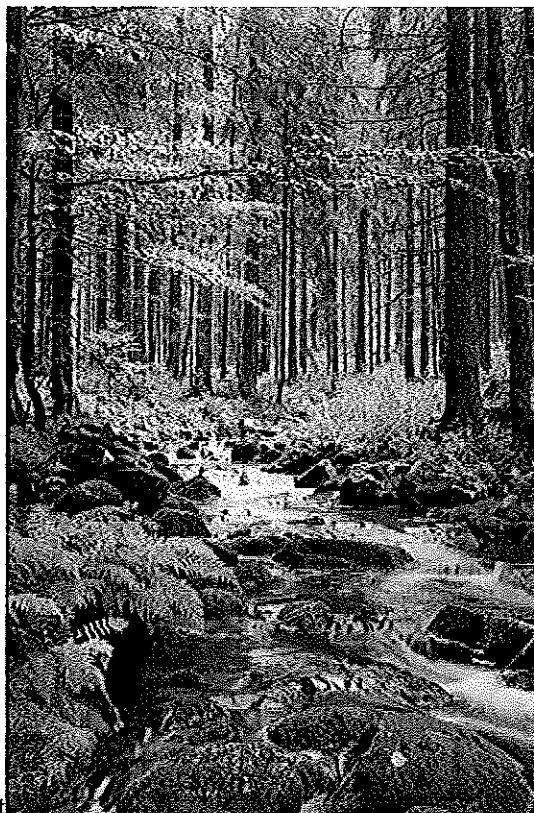


Carbon Friendly™ finances, supports and maintains global afforestation and reforestation projects. Afforestation/reforestation is simply the creation of new forests. Trees sequester carbon dioxide (the removal of carbon dioxide from the atmosphere) and store it in the wood and in the soil. Like a sponge is to water, a tree is to carbon dioxide. Forests actually remove existing carbon dioxide from the atmosphere, helping to clean up the existing global warming mess.

In addition to sequestering carbon, trees provide us with the clean air that we breathe. The leaves of trees act as a natural filter, absorbing other air pollutants such as carbon monoxide and sulfur dioxide. They also act a natural air conditioner, moderating our climate. Trees conserve water, protecting us from storm runoff and the possibility of flooding. Trees also harbor wildlife, attracting birds and other woodland animals.

Carbon Friendly™ ensures that all of its forestation projects are verified to meet the highest level of industry standards. Our methodologies, calculations and processes have been validated by reputable 3rd parties such as Kashue, Poland, the "National Administration of the Emission Trading Scheme" and by TÜV Rheinland.

List of Carbon Friendly™ Forestation Projects



Poland Afforestation Project

Phase I – Pilot Project

In 2007 Carbon Friendly and its wholly-owned subsidiary CO2 Reduction Poland Sp z.o.o had aggregated a total 50.74 hectares of private lands.

The project has been validated by TÜV Rheinland - to the International Standard Organization's ISO 14064-2 Specification for quantification, monitoring and reporting of greenhouse gas emission reductions or removal enhancements.

Phase II – Large Scale Implementation - Northern Poland Afforestation Offset Project

The Northern Poland Afforestation Offset Project areas contain an aggregate 4,823 hectares of privately owned lands in post agricultural, degraded conditions. These areas have been aggregated through extensive stakeholder consultations held by CO2 Reduction Poland ("CRP"), a wholly owned subsidiary of CFS. The project activity involves the planting of 24,248,614 trees, consisting of various native species on a 3,599 hectare portion of the total land area. The project activity is expected to generate approximately 1,517,025.804 tonnes of CO2 removals throughout its 40 year crediting period from the increased carbon stocks in natural carbon sinks (biomass growth and soil carbon retention). GHG removal enhancements by the project are equal to the sum of removals by aboveground biomass, belowground biomass and soils. Individual species' growth models were developed by the team from Warsaw University Life Sciences, Faculty of Forestry, Independent Division on Dendrometry and Forest Productivity ("SGGW") led by Mr. Michal Zasada, Ph.D., Dean of the Faculty of Forestry. The National Forest Inspectorate, the SGGW, and the CRP Monitoring Team shall monitor the afforestation to document growth and survival, mitigate potential carbon reversals, and ensure the successful establishment of "forests" within the project boundaries.

Conestoga-Rovers & Associates ("CRA") was retained to conduct the validation on February 25th, 2011, with the objective of providing assurance to CFS that the Project Documents have been developed in accordance with the validation criteria.

The Project has been validated to ensure the emission reduction quantities asserted, equivalent to 1,517,025 high-quality VERs, accurately portray methodologies and criteria specified by the ISO 14064-2, IPCC Good Practice Guidance for Land Use, Land-Use Change and Forestry 2003, and the UNFCCC approved consolidated afforestation and reforestation baseline and monitoring methodology AR-ACM001: "Afforestation and Reforestation of Degraded Land, Version 4".

The Project will be listed on the Markit Environmental Registry. The Markit Environmental Registry is a financial market based registry that allows accountholders to manage all their environmental credits in one common platform. The registry is linked with a number of carbon exchanges including the Carbon Trade Exchange ("CTX"). The CTX is a trusted marketplace where businesses can buy emissions commodities with confidence in the quality and origin of the products being sold. The Project's 1,517,025 high-quality VERs are expected to obtain the average 2010 over-the-counter price of \$6 USD per VER (Back to the Future, "State of the Voluntary Carbon Markets 2011").

MicroCoal

On January 31, 2011 the Company announced it had finalized the acquisition of 58.21% of the outstanding share capital of MicroCoal Inc. ("MicroCoal" or "MicroCoal"), as announced on January 12, 2011 and October 26, 2010. In accordance with the 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 Company (the "Share Exchange"). In addition to the Share Exchange and in accordance with the share purchase agreement, the Company is to complete a private placement financing of up to CAD\$6 million (the "Financing") and from such proceeds, the Company is to pay (i) US\$1 million cash to a certain creditor/shareholder of MicroCoal in consideration for the forgiveness of certain outstanding debt owed to such creditor by MicroCoal and for the re-purchase of such creditor's 1,013 MicroCoal shares for cancellation; and (ii) up to US\$85,000 cash to certain other creditors of MicroCoal to settle other outstanding indebtedness owed by MicroCoal. Upon completion of the entire transaction, the Company will own 100% of MicroCoal.

MicroCoal Inc. is a clean energy company focusing on commercializing the use of its patented technologies to decontaminate and upgrade low-rank coals to match the energy levels of high-rank coals

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for use by power utilities. MicroCoal Inc.'s proprietary on-site process not only cleans up coal at the power plant prior to combustion by significantly reducing contaminants, but it also reduces GHG emissions and improves fuel efficiency. The reduction in emissions allows for the generation of substantial carbon credits in an industry that is one of the world's largest producers of emissions. The deployment of MicroCoal's technology offers utilities significant economic, environmental as well as operational benefits. MicroCoal's website address: www.MicroCoal.com

MicroCoal, currently headquartered in Denver, CO with its pilot plant located in Golden, CO, is focused on reducing CO₂ emissions in coal-fired plants by commercializing the use of microwave energy and its related patented technologies to upgrade low-rank, i.e. sub-bituminous and lignite coals to match the energy levels of high-rank, i.e. bituminous coals, for use by power utilities. MicroCoal's proprietary on-site process not only cleans up coal at the power plant prior to combustion by reducing contaminants like sulfur and mercury, but it also reduces CO₂ emissions and improves fuel efficiency by removing water.

MicroCoal's proprietary clean coal technology has significant growth potential into multiple geographies and various industrial markets. Its business model is based on licensing the technology with a once-off *technology fee* and an annual maintenance fee derived of the initial project costs.

On December 15, 2011 the Company and its subsidiary MicroCoal announced that Ameren has signed a Letter of Interest ("LOI") that reflects the intention of Ameren Corporation (NYSE:AEE) ("Ameren") and MicroCoal to negotiate a term sheet and enter into a proposed license agreement relating to the deployment of MicroCoal technology at one of Ameren's coal-fired power plants (the "Nominated Plant") in two main phases.

The first phase is proposed to commence in January, 2012 and consists of re-configuring MicroCoal's four year old pilot plant in Colorado to determine the design for Ameren's plant in upgrading Powder River Basin (PRB) coal to higher energetic value (BTU rating). The second phase involves the construction and operation of a fully integrated commercial plant, which will be able to treat 250,000 tons of PRB coal per month. This first commercial coal upgrading plant will be located at Ameren's Nominated Plant, located in the State of Missouri. It is a 1,000 Megawatt coal-fired plant and burns approximately 3 million tons of coal annually. The Nominated Plant is one of the largest among the 11 coal-fired plants owned by Ameren. Using the internationally patented MicroCoal process, an MicroCoal plant located on-site of the coal power generation station uses the station's off-peak slack electricity capacity to remove large amount of water from coal, and increase the BTU rating of the coal. The technology also has the ability to remove contaminants, in addition to allowing utilities to use PRB coal without suffering a loss in generation capacity (derate). PRB coal contains lower contaminant levels (such as sulfur) than the higher BTU Eastern coals, such as Illinois Basin (ILB) coal. When compared to raw coal from Montana and Wyoming's Powder River Basin, MicroCoal treated coal at the Nominated Plant will have approximately 15 percent more energetic value in addition to reductions in carbon dioxide, mercury, sulfur dioxide, and nitrous oxides. Results will vary based on the type and source of the coal.

On December 22nd, 2011 the Company reached an agreement with Orica Limited (ASX:ORI) ("ORI" or the "Recipient") defining the terms and obligations for the settlement of ORI's outstanding debt in MicroCoal and the transfer of its remaining 41.79% stake in MicroCoal to the Company (the "Debt").

Pursuant to the Share Purchase Agreement signed by Carbon Friendly and ORI on October 15th, 2010 sanctioning Carbon Friendly's acquisition of the majority share capital in MicroCoal (58.21%), and the amendment to the agreement signed on January 10th, 2011, allowing Carbon Friendly to acquire ORI's remaining debt and security interest in MicroCoal for USD\$1,000,000, giving the Company full ownership of MicroCoal; the Voluntary Emission Reduction Transfer Agreement (the "Agreement") was drafted to outline the terms, obligations and execution schedule of the Secured Convertible Promissory Note. The Voluntary Emission Reduction Transfer Agreement consigns to Carbon Friendly providing ORI with (i) a

down payment of USD\$125,000, (ii) the transfer of 200,000 VERs from Carbon Friendly's Offset Inventory, and (iii) a final payment for any shortfall from the remaining debt.

The VERs represented in the Agreement will consist of ISO 14064-2 Validated Voluntary Emission Reductions generated from the Northern Poland Afforestation Offset Project ("NPAOP") as a security on the payment of the Debt. Carbon Friendly will transfer all legal and equitable title of the VERs to ORI through an accredited registry account permitting ORI to engage in selling the VERs to other entities or retiring the VERs as a signal to reducing its own global carbon footprint. Upon settlement of the Voluntary Emission Reduction Transfer Agreement, ORI will have no remaining debt in MicroCoal, priority interest in any of MicroCoal's assets, or ownership shares MicroCoal. Carbon Friendly will hold a full ownership stake (100% shareholding) of MicroCoal.

MicroCoal Technology

Coal is classified by quality, based on its heat value (BTU rating), into two main categories and four different types as follows:

- High-rank, including anthracite and bituminous
- Low-rank, including sub-bituminous and lignite

Thermal coal used by utilities includes bituminous, sub-bituminous and lignite coals. The heat value of coal is directly dependent on its moisture content: the lower the moisture – the higher the coal's heat value. Generally speaking, low-rank coals are younger and cleaner than high-rank coals, and a lot cheaper.

MicroCoal's patented technology suite revolves around the use of microwave energy to dewater and upgrade low-rank coals. In addition to microwave, MicroCoal has developed supplementary processes to further remove contaminants and CO₂, and produce an efficient power plant fuel from available raw coal.

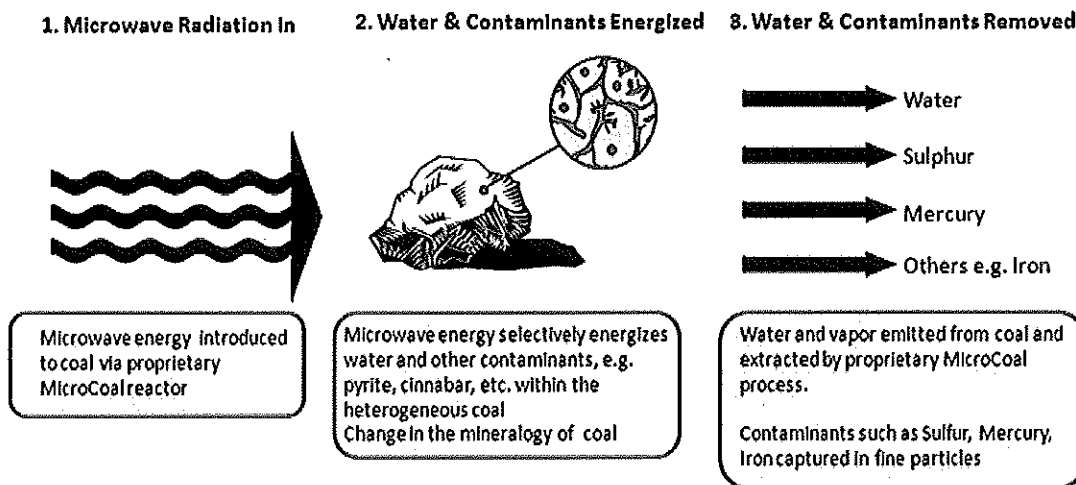


Figure 1: How it works

The Benefits of MicroCoal's Process

According to the World Coal Institute, up to 5% of the carbon footprint of utilities can be eliminated by drying the coal prior to combustion. A further 22% of CO₂ emission can be reduced, improving generation efficiency. The direct result of this is a worldwide interest in clean coal and coal drying technologies, which is the focus of the MicroCoal's business initiative.

The deployment of MicroCoal Inc.'s technology will give the utility three main benefits:

- ✓ **Environmental benefits**, due to a significant reduction of coal contaminants and CO₂ emission;
- ✓ **Economic benefits**, due to fuel switch from expensive high-rank coal to cheaper low-rank coal and with increased heat value of the latter, as well as additional revenue from generating carbon offsets;
- ✓ **Operational benefits**, due to marked change of slagging and ash build-up.

The combined benefits of the MicroCoal's technology suite has been discussed with utilities, experts in the field, industry consultants and coal analysts, all of whom have indicated support for the approach. Indications are that, once funding has been secured, various utilities will be prepared to sign collaboration agreements with a view to applying the technology once its development is complete.

Typical 500 MW Coal-Fired Power Plant Indicative Benefits

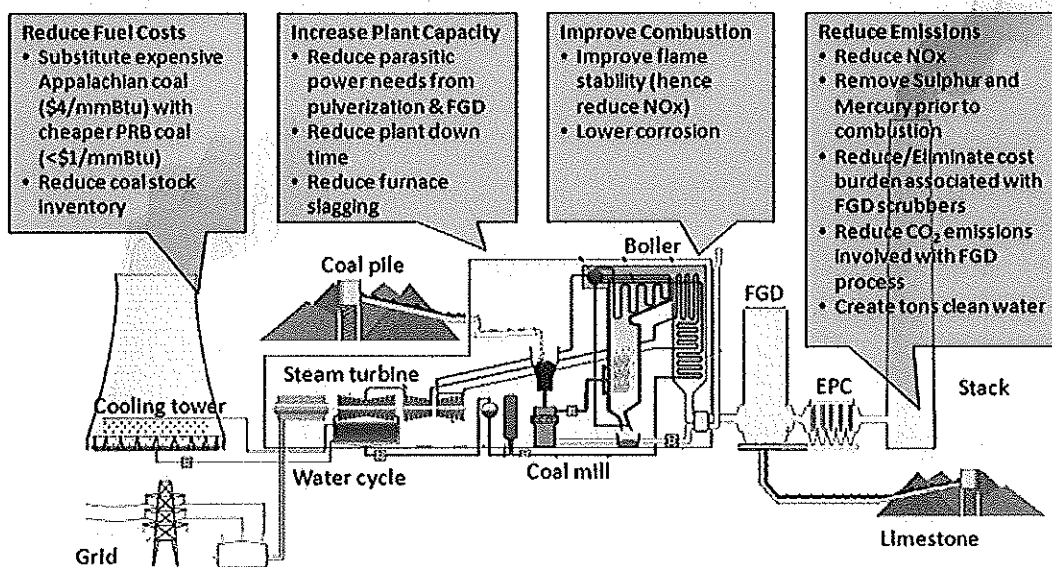


Figure 2: Indicative Benefits

MicroCoal Market Opportunity

Coal is, and will continue to be, an indispensable part of the global energy mix. However, coal requires innovation to enhance its long term appeal by improving its emissions profile and improving the efficiency of coal as a source of fuel. Over 4030 Mt¹ of coal is currently produced globally and is expected to reach 7 billion tonnes in 2030 – with China accounting for around half the increase over this period. The top five producers are China, the USA, India, Australia and South Africa. Coal currently fuels 39% of the world's electricity and this proportion is expected to remain at similar levels over the next 30 years. The biggest

¹ World Coal Institute

market for coal is Asia, which currently accounts for 54% of global coal consumption – although China is responsible for a significant proportion of this.

The U.S. Market

Approximately 1,100 million tons of coal is consumed in the U.S. every year to generate 50% of the electricity in the country. The introduction of the Clean Air Act of 1990, and the Clean Air Act Amendment ("CAAA") in 2000 forced utilities to control their emissions to meet with US Environmental Protection Agency ("EPA") standards. Utilities are faced with two options for controlling emissions:

- Change fuel to low sulfur coal such as PRB coal, which is the cheaper option;
- Deploy high capacity post combustion control systems such as flue-gas desulfurization ("FGD"), mostly scrubbers, which is a very expensive option.

A combination of the above two options could also be applied. Approximately 40% of generation units have deployed FGD, while many have switched to PRB coal, as is evident in its spectacular growth. The other alternative for a plant is to deploy MicroCoal's technology, which will upgrade PRB coal to the heat value equivalent to high-ranking coal, thereby allowing utilities to benefit from the significant lower input costs, while at the same time enjoying the environmental benefits of reduced CO₂, SO₂ and mercury emissions. In 2007 the fleet of U.S. coal-fired power generation consisted of over 1,400 units in various sizes. Of these units, 950 are designed to burn bituminous coal. These are the potential candidates for MicroCoal's technology. The immediate market segment for MicroCoal has been identified as those generation units with the capacity of 200MW and less, which totals over 600 units. The reasons for selecting this initial target market are:

- Smaller units are under pressure to come in-line with more stringent environmental standards, and are more threatened with closure than larger units.
- These units are typically older, and generally do not have space available to deploy traditional environmental control facilities such as FGD, which require large areas.

The second market segment, which will be addressed by MicroCoal are those units with a capacity of 500MW and higher, and emerging markets such as China and India will be the third market.

International Market

The worldwide installed base of coal-fired power generation is expected to grow by 67% by 2020. 80% of the growth will come from China and India. China alone accounts for over two-thirds of this growth. The price spread and quality difference between low-rank and high-rank coals in the rest of the world is similar to that of the U.S. MicroCoal has tested Indonesian coal in its facilities, and showed that its technology is as applicable to international coals as it is to U.S. coals.

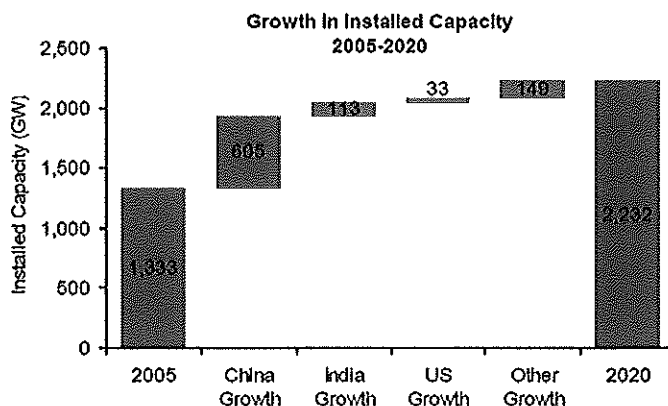


Figure 3: Global growth of coal-fired power generation in GW²

Financial Plan and Milestones

Carbon Friendly's financial plan for MicroCoal addresses the following two of four development phases, which mark the milestones deemed critical to successfully commercialize MicroCoal's proprietary technologies. During the next 12 months Carbon Friendly will focus on the completion of MicroCoal's Phase I and Phase II development stages.

The Company is confident it can raise the required future funding for completion of the commercialization Phases III and IV stages through public equity, available government grants and licensing arrangements with existing coal fired facilities interested in utilizing the MicroCoal technology.

Marketing and Sales

Emission Reduction Offsets

Typically emission offsets are sold utilizing the services of emission brokers who take orders or requests from clients looking for particular emission offsets. Carbon Friendly has established ongoing relationships with many different emission brokers and traders and has regular dialogue to ensure all parties are aware of projects Carbon Friendly is developing and timing of obtaining validation for sale of offsets.

With the recent successful launch of the Markit Environmental Registry (<http://www.tz1market.com/>) Carbon Friendly can now register all land based sequestration projects to obtain greater public exposure and facilitate timely sales of project offsets. In addition projects listed on the Markit Registry provide full project transparency and because all offset purchases are recorded and retired, it gives assurance of no double counting to all potential buyers.

The Carbon Friendly company website includes its proprietary carbon footprint calculator and option to purchase Carbon Friendly carbon credits directly from the website. The Company is selling carbon credits on the website to individuals and small businesses for \$12.50 USD per carbon credit. Carbon Friendly intends to increase its branding and awareness on the Internet through key word pay-per-click advertising on Google and linking to other environmental sites.

² Characteristics of the Worldwide Coal Fleet: Implications for CCS Retrofit RD&D The NorthBridge Group MIT Symposium on CCS Retrofit Technology Cambridge, MA March 23, 2009

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With respect to carbon accounting, voluntary reforestation project proponents typically use ex-ante accounting for forestry activities, meaning that the carbon dioxide removals in the future are sold before they actually occur. This practice is accepted by buyers and defended on the basis that most of the costs are incurred in the early years of a forestry project; therefore, "ex-post" accounting (selling the reductions after they have occurred over the life of the project) is simply not economically viable.

In the unlikely scenario of an unexpected event causing damage to the project, Carbon Friendly establishes a buffer or reserve inventory to ensure and guarantee the delivery of offsets. This varies depending on the risk analysis of the project site location but typically the Company creates a minimum 10% buffer or offset reserve that remains in an inventory reserve account for the life of the project.

CARBIOPEL

The Company executed a share purchase agreement with the shareholders of Carbiopel - Eco Stream Power S.A. ("Carbiopel") pursuant to which the Company can 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 injections of up to two million zloty to develop a business model in Poland.

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, from the issuance of 400,000 common shares in the capital of the Company (market price on the day the shares were issued was \$0.27 per share).

An advance of \$62,000 was made to Carbiopel to initiate the business plan.

1.3 Selected Annual Information

Selected annual information from the consolidated audited financial statements for the three years ended is summarized as follows:

| June 30, | 2011 | 2010 | 2009 |
|-----------------------------|-------------|-------------|-------------|
| Revenues | \$7,980 | \$45,194 | \$35,072 |
| Gross profit (loss) | (1,587) | (33,822) | 8,796 |
| Operating expense | 3,505,033 | 2,482,956 | 1,636,226 |
| Other income (expense) | 105,473 | (93,651) | 17,659 |
| Net loss for the period | (3,401,842) | (2,610,429) | (1,609,771) |
| Net loss per share | (0.09) | (0.11) | (0.09) |
| Total assets | 6,571,738 | 420,568 | 802,016 |
| Total long-term liabilities | Nil | Nil | Nil |
| Cash dividends declared | Nil | Nil | Nil |

1.4 Results of Operations

During the quarter ended September 30, 2011, the Company incurred a loss of \$1,141,668 or \$0.03 per share compared to a loss of \$461,262 or \$0.02 per share for the comparable year, an increase of \$395,725.

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Consulting fees were incurred in regards to operations in Poland for \$42,000 locating carbon credit afforestation/reforestation land and obtaining verification credits, hiring of a firm providing capital growth advice for \$10,000, and coal technology for 88,656. Share based compensation has been charged \$59,600 in regards to the vesting of share options vesting in the 1st quarter. Interest on notes payable is in reference to loans in MicroCoal.

Amortization of the coal pilot plant on a 20% straight line basis added \$742,648 to amortization expense.

Under IFRS foreign exchange is separated into two categories. The first is foreign exchange loss (gain) on operations reflecting business transactions throughout the quarter. Under IFRS a determination of the functional currency(ies) was made with the result that the assets and liabilities were translated at closing foreign rates at the time of the financial statement as compared to Canadian GAAP where historical rates were applied for previously recognized amounts. Expenses were translated at average exchange rates in both IFRS and Canadian GAAP. Exchange gains and losses arising on translation of foreign assets and liabilities is shown separately under other comprehensive income.

The foreign exchange rates of the Canadian dollar compared to the Polish zloty was:

| Date | End of period | Average |
|--------------------|---------------|---------|
| June 30, 2010 | 3.2514 | 2.79988 |
| September 30, 2010 | 2.8774 | 2.8392 |
| December 31, 2010 | 3.0014 | 2.9653 |
| March 31, 2011 | 2.9141 | 2.9268 |
| June 30, 2011 | 2.8254 | 2.9058 |
| September 30, 2011 | 3.1441 | 2.9854 |

The foreign exchange rates of the Canadian dollar compared to the United States dollar:

| Date | End of period | Average |
|--------------------|---------------|---------|
| June 30, 2011 | 1.0212 | 0.9987 |
| September 30, 2011 | 1.0326 | 0.9780 |

1.5 Summary of Quarterly Results

| Quarter ended | Revenues | Other items | Net loss | Loss per share |
|--------------------|----------|-------------|-------------|----------------|
| September 30, 2011 | - | (127,698) | (1,141,668) | (0.03) |
| June 30, 2011 | 212 | 81,910 | (2,004,342) | (0.04) |
| March 31, 2011 | 7,102 | 4,808 | (549,734) | (0.02) |
| December 31, 2010 | 8 | 10,296 | (403,167) | (0.01) |
| September 30, 2010 | 658 | (37,972) | (444,599) | (0.02) |
| June 30, 2010 | 45,194 | (44,004) | (819,551) | (0.03) |
| March 31, 2010 | - | 15,736 | (620,545) | (0.03) |
| December 31, 2009 | - | (307) | (851,301) | (0.03) |

1.6/1.7 Liquidity and Capital Resources

The Company had cash on hand of \$266,644 at September 30, 2011 and a working capital deficiency of \$4,358,277. .

1st Quarter

A second tranche of a private placement announced on June 21, 2011 raised an additional \$1,099,000. The total financing was comprised of \$2,153,550 in gross proceeds from the subscription of 10,767,750 units. Each unit consisted of one common share and one common share purchase warrant to purchase one common share of the Company at an exercise price of \$0.35 per share for a period of two years. A first tranche was completed at June 30, 2011 with the balance of 5,495,000 units completed in the current quarter. Fees pursuant to the private placement of \$29,900 were incurred.

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 remained as share subscriptions receivable; which has been collected subsequent to year-end.

During the year ended June 30, 2011, the Company issued 395,000 shares on exercise of stock options for proceeds of \$84,850.

Pursuant to several loan agreements a total of \$425,000 was advanced to the Company. In regards to advances of \$385,000, a 20% loan bonus was charged with the loan amount calculated at \$462,000 to be repaid. Two additional loans for a total of \$40,000 had no bonus arrangements at 2% interest per month. In all other cases 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 \$300,000.

The Company is hopeful of completing additional equity financing in 2011-2012. Additional equity financing has been completed subsequent to year-end, see item 1.10, subsequent events.

The Company may continue to have capital requirements in excess of its currently available resources. In the event the Company's plans change, its assumptions change or prove inaccurate, or its capital resources in addition to projected cash flow, if any, prove to be insufficient to fund operations, the Company may be required to seek additional financing. Although the Company has been successful in raising the funds, there can be no assurance that the Company will have sufficient financing to meet its future capital requirements or that additional financing will be available on terms acceptable to the Company in the future.

1.8 Off-Balance Sheet Arrangements

The Company does not utilize off-balance sheet arrangements.

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1.9 Transactions with Related Parties

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

| | Three months ended September 30, 2011 | Three months ended September 30, 2010 |
|--|--|--|
| Key management personnel remuneration | | |
| Management and directors' fees | \$ 160,620 | \$ 20,125 |
| Consulting | 12,000 | 20,000 |
| Automobile allowance (travel and promotion) | 12,450 | 9,600 |
| Professional fees | 24,000 | 15,552 |
| Total key management personnel remuneration | 209,070 | 65,277 |
| Other | | |
| Rent | - | 3,000 |
| Total | \$ 209,070 | \$ 68,277 |

As at September 30, 2011 accounts payable and accrued liabilities included \$201,063 (June 30, 2011 - \$440,646) owing to officers and directors for management and accounting fees. 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 in the normal course of operations and were measured at the exchange amount which is the amount of consideration established and agreed to by the related parties.

1.10 Subsequent events

Share subscriptions

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

Coal technology and plant prototype

The Company has arranged a purchase of the 41.79% in MicroCoal held by Orica (note 6). The Company will pay the sum of \$125,000 USD immediately and a balance of \$875,000 USD by March 31, 2012. The Company has to transfer 200,000 VERS (Verified Emission Reductions) (note 12) for use by Orica where sale proceeds would be subtracted from the balance owing of \$875,000 USD.

The Company announced that Ameren Corporation (NYSE:AEE) ("Ameren") has signed a Letter of Interest ("LOI") that reflects the intention of Ameren and MicroCoal to negotiate a term sheet and enter into a proposed license agreement relating to the deployment of MicroCoal technology at one of Ameren's coal-fired power plants (the "Nominated Plant") in two main phases. The first phase is proposed to commence in January, 2012 and consists of re-configuring MicroCoal's pilot plant in Colorado to determine the design for Ameren's plant in upgrading Powder River Basin (PRB) coal to higher energetic value (BTU rating). The second phase involves the construction and operation of a fully integrated commercial plant, which will be able to treat 250,000 tons of PRB coal per month. This first commercial coal upgrading plant will be located at Ameren's Nominated Plant, located in the State of Missouri. It is a 1,000 Megawatt coal-fired plant and burns approximately 3 million tons of coal annually.

Debt settlement

The Company issued 150,000 common shares in settlement of a debt.

1.11 Adoption of New Accounting Standards

Statement of Compliance

These interim financial statements are unaudited and have been prepared in accordance with IAS 34 'Interim Financial Reporting' ("IAS 34") using accounting policies consistent with the International Financial Reporting Standards ("IFRS") issued by the International Accounting Standards Board ("IASB") and Interpretations of the International Financial Reporting Interpretations Committee ("IFRIC").

The policies applied in these interim financial statements are based on IFRS issued and effective for the year ended June 30, 2012. Any subsequent changes to IFRS that are given effect in the annual financial statements for the year ending June 30, 2012 could result in restatement of these interim financial statements, including the transition adjustments recognized on change-over to IFRS.

These are the Company's first IFRS interim financial statements for part of the period covered by the Company's first IFRS annual financial statements for the year ending June 30, 2012. Previously, the Company prepared its annual and interim financial statements in accordance with Canadian Generally Accepted Accounting Principles ("GAAP"). The explanation of the effect of the transition to IFRS is set the financial statements for the period ended September 30, 2011.

As these are the Company's first set of interim financial statements in accordance with IFRS, the Company's disclosures exceed the minimum requirements under IAS 34. The Company has elected to exceed the minimum requirements in order to present the Company's accounting policies in accordance with IFRS and the additional disclosures required under IFRS, which also highlight the changes from the Company's 2011 annual financial statements prepared in accordance with Canadian GAAP. In 2012 and beyond, the Company may not provide the same amount of disclosure in the Company's interim financial statements under IFRS as the reader will be able rely on these and the annual financial statements which will be prepared in accordance with IFRS.

FUTURE IFRS STANDARDS AND INTERPETATIONS ISSUED BUT NOT YET EFFECTIVE

Unless otherwise indicated below, the Company is in the process of assessing whether there will be any significant impact on its consolidated financial statements upon future adoption of these new standards, interpretations, or amendments. At this time, the Company does not plan to early adopt any of these new standards, interpretations, or amendments.

Financial instruments

The IASB intends to replace IAS 39 - Financial Instruments: Recognition and Measurement ("IAS 39") in its entirety with IFRS 9 - Financial Instruments ("IFRS 9") in three main phases. IFRS 9 will be the new standard for the reporting of financial instruments that is principles-based and less complex than IAS 39. IFRS 9 retains but simplifies the mixed measurement model and establishes two primary measurement categories for financial assets: amortized cost and fair value. The basis of classification depends on the entity's business model and the contractual cash flow characteristics of the financial asset. The standard is effective for annual periods beginning on or after January 1, 2015. The Company is in the process of evaluating the impact of the new standard on the accounting for the available-for-sale investment.

Consolidation

In May 2011, the IASB issued IFRS 10 - Consolidated Financial Statements ("IFRS 10"), which supersedes SIC 12 and the requirements relating to consolidated financial statements in IAS 27 - Consolidated and Separate Financial Statements. IFRS 10 is effective for annual periods beginning on or after January 1, 2013, with earlier application permitted under certain circumstances. IFRS 10 establishes control as the basis for an investor to consolidate its investees; and defines control as an investor's power

over an investee with exposure, or rights, to variable returns from the investee and the ability to affect the investor's returns through its power over the investee.

In addition, the IASB issued IFRS 12 - Disclosure of Interests in Other Entities ("IFRS 12") which combines and enhances the disclosure requirements for the Company's subsidiaries, joint arrangements, associates and unconsolidated structured entities. The requirements of IFRS 12 include reporting of the nature of risks associated with the Company's interests in other entities, and the effects of those interests on the Company's consolidated financial statements. One of the most significant changes introduced by IFRS 12 is that an entity is now required to disclose the judgments made to determine whether it controls another entity.

Concurrently with the issuance of IFRS 10, IAS 27 and IAS 28 - Investments in Associates ("IAS 28") were revised and reissued as IAS 27 - Separate Financial Statements and IAS 28 - Investments in Associates and Joint Ventures to align with the new consolidation guidance.

Interests in joint ventures

In May 2011, the IASB issued IFRS 11 - Joint Arrangements ("IFRS 11"), which supersedes IAS 31 - Interests in Joint Ventures and SIC-13 - Jointly Controlled Entities - Non-Monetary Contributions by Venturers. IFRS 11 is effective for annual periods beginning on or after January 1, 2013, with earlier application permitted under certain circumstances. Under IFRS 11, joint arrangements are classified as joint operations or joint ventures based on the rights and obligations of the parties to the joint arrangements. A joint operation is a joint arrangement whereby the parties that have joint control of the arrangement ("joint operators") have rights to the assets, and obligations for the liabilities, relating to the arrangement. A joint venture is a joint arrangement whereby the parties that have joint control of the arrangement ("joint venturers") have rights to the net assets of the arrangement. IFRS 11 requires that a joint operator recognize its portion of assets, liabilities, revenues and expenses of a joint arrangement, while a joint venturer recognizes its investment in a joint arrangement using the equity method.

Fair value measurement

In May 2011, IASB issued IFRS 13 - Fair Value Measurement. The standard defines fair value and sets out a single framework for measuring fair value and requires disclosure about fair value measurements. IFRS 13 is effective for annual periods beginning on or after January 1, 2013, with earlier application permitted. IFRS 13 requires entities to disclose information about the valuation techniques and inputs used to measure fair value, as well as information about the uncertainty inherent in fair value measurements. The Company does not anticipate the application of IFRS 13 to have a material impact on its consolidated financial statements.

Financial statement presentation

In June 2011, the IASB issued amendments to IAS 1 - Presentation of Financial Statements ("IAS 1") that require an entity to group items presented in the other comprehensive income (OCI) on the basis of whether they may be reclassified to profit or loss subsequent to initial recognition. The amendments are effective for annual periods beginning on or after July 1, 2012, with earlier adoption permitted. The Company does not anticipate the application of the amendments to IAS 1 to have a material impact on its consolidated financial statements.

1.12 Financial Instruments and Risks

As at September 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.

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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.

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 19.

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:

| | United States | | Poland | |
|--|--------------------|---------------|--------------------|---------------|
| | September 30, 2011 | June 30, 2011 | September 30, 2011 | June 30, 2011 |
| Cash | 61,777 | 1,987 | 7,626 | 312 |
| Accounts payable and accrued liabilities | (1,619,269) | (1,310,995) | (70,186) | (71,503) |
| Related parties | (162,629) | (99,715) | (17,115) | (19,045) |
| Loans payable | (2,323,350) | (2,203,200) | - | - |
| | (4,043,471) | (3,611,923) | (79,675) | (90,236) |

The following exchange rates were applied:

| | Three months ended September 30, 2011 | | Year ended June 30, 2011 | |
|--|---------------------------------------|-----------|--------------------------|-----------|
| | Average rate | Spot rate | Average rate | Spot rate |
| | | | | |

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| | | | | |
|--------------------------------|--------|--------|--------|--------|
| Canadian dollars to US dollars | 0.9780 | 1.0326 | 0.9987 | 1.0212 |
| Canadian dollars to Zloty | 2.9854 | 3.1441 | 2.9058 | 2.8254 |

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.

1.13 Other Requirements

Summary of Outstanding Share Data as at December 27, 2011

Authorized – 100,000,000 shares without par value

| | |
|----------------------------|------------|
| Issued | |
| September 30, 2011 | 50,078,955 |
| Issued | 150,000 |
| Total at December 27, 2011 | 50,228,955 |

| | |
|----------------------------|-----------|
| Stock options | |
| September 30, 2011 | 4,391,620 |
| Options granted | 630,000 |
| Total at December 27, 2011 | 5,021,620 |

| | |
|----------------------------|------------|
| Warrants | |
| September 30, 2011 | 20,515,450 |
| Expired | 7,675,200 |
| Total at December 27, 2011 | 12,840,250 |

Additional disclosures pertaining to the Company's management information circulars, material change reports, press releases and other information are available on the SEDAR website at www.sedar.com.