CARBON FRIENDLY SOLUTIONS INC.

Consolidated Condensed Interim Financial Statements

Six months ended December 31, 2012

(in Canadian dollars)

CARBON FRIENDLY SOLUTIONS INC.

Unaudited Consolidated Condensed Interim Financial Statements
December 31, 2012

Notice of No Auditor Review of Interim Condensed Financial Statements

The accompanying unaudited consolidated condensed interim financial statements have been prepared by management and have not been the subject of a review by the Company's external independent auditors.

CARBON FRIENDLY SOLUTIONS INC.
Consolidated Condensed Interim Statement of Financial Position
(in Canadian dollars)

	Note	December 31, 2012	June 30, 2012
ASSETS			
Current			
Cash		$ 612,817	$ 31,292
Receivables	7	91,217	229,818
Prepaid expenses		20,869	45,277
		724,903	306,387
Non-current			
Deposit	9	56,729	56,729
Property and equipment	8	401,027	418,335
Coal technology and plant prototype	6	4,352,556	5,058,487
Intangibles	11	4,365	49,574
Total assets		$ 5,539,580	$ 5,889,512
LIABILITIES			
Current			
Accounts payable and accrued liabilities	12	$ 2,178,500	$ 2,031,378
Related parties	15	328,330	354,817
Loans payable	13	2,281,280	2,453,370
		4,788,110	4,839,565
SHAREHOLDERS' EQUITY			
Share capital	14b	13,749,125	12,013,125
Share subscription receivable	14b	(28,000)	-
Share-based payment reserve	14f	1,955,439	1,743,317
Deficit		(15,142,280)	(12,746,255)
Cumulative other comprehensive income		(21,964)	(199,390)
		512,320	810,797
Non-controlling interest		239,150	239,150
Total equity		751,470	1,049,947
Total liabilities and equity		$ 5,539,580	$ 5,889,512

Approved on behalf of the Board:

"Slawomir Smulewicz"
Director

"Stan Lis"
Director

CARBON FRIENDLY SOLUTIONS INC.

Consolidated Condensed Interim Statements of Comprehensive Loss

(in Canadian dollars)

	Note	Three months ended December 31, 2012	Three months ended December 31, 2011	**Six months ended December 31, 2012**	Six months ended December 31, 2011
Expenses					
Amortization		$ 382,161	$ 445,710	$ 751,058	$ 894,282
Bank charges and interest		4,618	972	6,004	2,453
Consulting fees	15	302,620	42,435	409,499	240,834
Finance and sponsorship fees		-	-	-	852
Foreign exchange loss (gain) on operations		33,852	(4,836)	30,801	(4,978)
Interest on notes payable		78,289	44,949	126,913	161,773
Investor relations		19,369	16,513	33,816	34,224
Management and director fees	15	173,925	205,000	288,732	276,864
Office and miscellaneous		43,650	12,227	56,642	77,216
Professional fees	15	147,194	164,130	222,563	235,745
Rent		27,194	38,455	55,840	79,919
Share-based compensation		212,122	158,979	212,122	218,579
Transfer agent and regulatory fees		7,531	7,409	9,819	11,055
Travel and promotion	15	66,412	33,024	95,542	56,736
Wages and benefits		25,304	38,263	57,238	59,244
Write down of goodwill		-	-	48,897	-
Write down (recovery) of receivable		(240)	-	(13,621)	-
		(1,524,001)	(1,203,230)	(2,391,865)	(2,344,798)
Loss for the period		(1,524,001)	(1,203,230)	(2,391,865)	(2,344,798)
Loss on disposal of capital assets		(4,160)	(37,143)	(4,160)	(37,143)
		(4,160)	(37,143)	(4,160)	(37,143)
		(1,528,161)	(1,240,373)	(2,396,025)	(2,381,941)
Other comprehensive income (loss)					
Exchange gain (loss) arising on translation of foreign operations		(33,186)	90,555	177,426	(37,143)
		(33,186)	90,555	177,426	(37,143)
Total comprehensive income (loss)		$ (1,561,347)	$ (1,149,818)	$ (2,218,599)	$ (2,419,084)
Loss for the period attributable to:					
Owners of parent		$ (1,767,311)	$ -	$ (2,396,025)	$ (888,418)
Non-controlling interest		-	-	-	(253,250)
		$ (1,528,161)	$ (1,240,373)	$ (2,396,025)	$ (2,381,941)
Total comprehensive loss attributable to:					
Owners of parent		$ (1,800,497)	$ -	$ (2,218,599)	$ (1,016,116)
Non-controlling interest		-	-	-	(253,250)
		$ (1,561,347)	$ (1,149,818)	$ (2,218,599)	$ (2,419,084)
Loss per share, basic and diluted		$ (0.03)	$ (0.03)	$ (0.04)	$ (0.03)

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

CARBON FRIENDLY SOLUTIONS INC.
Consolidated Condensed Interim Statements of Cash Flows
(in Canadian dollars)

	Note	Six months ended December 31, 2012	Six months ended December 31, 2011
Cash provided by (used in):			
Operating Activities			
Net loss for the period		$ (2,396,025)	$ (2,381,941)
Items not involving cash:			
Amortization		751,058	894,282
Loss on disposal of capital assets		4,160	-
Share-based compensation		212,122	218,579
Unrealized foreign exchange loss		64,936	-
Accrued interest expense		35,924	-
Impairment of goodwill		48,897	-
		(1,278,928)	(1,269,080)
Change in non-cash working capital:			
Receivables		138,601	(13,419)
Prepaid expenses and deposits		24,408	(5,105)
Accounts payable and accrued liabilities		136,854	37,601
Related parties		(27,061)	-
		(1,006,126)	(1,250,003)
Investing Activities			
Purchase of property and equipment		(3,408)	-
Purchase of intangible assets		-	(102,000)
		(3,408)	(102,000)
Financing Activities			
Share issuances		1,734,750	1,099,000
Issue costs		(26,750)	(29,900)
Share subscriptions		-	352,000
Loan proceeds		30,000	125,000
Loan repayments		(148,715)	(137,258)
		1,589,285	1,408,842
Effect of foreign exchange		1,774	2,305
Increase in cash		581,525	59,144
Cash, beginning of year		31,292	3,031
Cash, end of period		$ 612,817	$ 62,175
Supplemental cash flow information:	5		

CARBON FRIENDLY SOLUTIONS INC.

Consolidated Condensed Interim Statements of Equity

(in Canadian dollars)

	Shares	Amount	Share subscriptions	Share-based payment reserves	Deficit	Cumulative other comprehensive income	Non-controlling interest	Total
Balance, July 1, 2011	44,183,955	$ 8,650,892	$ (352,000)	$ 1,698,955	$ (9,703,060)	$ 104,778	$ 1,436,685	$ 1,836,250
Share issuances								
Private placement	5,495,000	1,099,000	(364,500)	-	-	-	-	734,500
Issue costs	-	(29,900)	-	-	-	-	-	(29,900)
Shares issued for acquisition of Carbiopel	400,000	108,000	-	-	-	-	-	108,000
Share subscriptions	-	-	352,000	-	-	-	-	352,000
Share-based compensation	-	-	-	59,600	-	-	-	59,600
Loss for the period	-	-	-	-	(888,418)	-	(253,250)	(1,141,668)
Comprehensive loss	-	-	-	-	-	(127,698)	-	(127,698)
Balance, December 31, 2011	50,078,955	9,827,992	(364,500)	1,758,555	(10,591,478)	(22,920)	1,183,435	1,791,084

	Shares	Amount	Share subscriptions	Share-based payment reserves	Deficit	Cumulative other comprehensive income	Non-controlling interest	Total
Balance, July 1, 2012	58,231,721	$ 12,013,125	$ -	$ 1,743,317	$ (12,746,255)	$ (199,390)	$ 239,150	$ 1,049,947
Share issuance								
Private placement	8,673,750	1,734,750	(28,000)	-	-	-	-	1,706,750
Issue costs	-	(26,750)	-	-	-	-	-	(26,750)
Share-based compensation	-	-	-	212,122	-	-	-	212,122
Stock options	200,000	28,000	-	-	-	-	-	28,000
Loss for the period	-	-	-	-	(2,396,025)	-	-	(2,396,025)
Other comprehensive income	-	-	-	-	-	177,426	-	177,426
Balance, December 31, 2012	67,105,471	$ 13,749,125	$ (28,000)	$ 1,955,439	$ (15,142,280)	$ (21,964)	$ 239,150	$ 751,470

1. NATURE OF OPERATIONS

Carbon Friendly Solutions Inc. ("Carbon Friendly" or "the Company") was incorporated on April 6, 1990 under the laws of the Province of British Columbia. The Company's head office is located at 2500 - 555 West Hastings Street, Vancouver, British Columbia, Canada, V6B 4N5.

The Company is a reporting issuer in the provinces of Alberta, British Columbia and Ontario and the Company's shares are listed for trading on the Canadian National Stock Exchange (the 'CNSX") under the symbol "CFQ".

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, via its subsidiary in U.S., is also providing coal technology using patented technologies to decontaminate and upgrade low-rank coals for use by power utilities.

2. BASIS OF PREPARATION

(a) Statement of Compliance

These consolidated condensed interim financial statements have been prepared by management and reported in Canadian dollars in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("ASS") applicable to the preparation of interim financial statements, including International Accounting Standard 34, "Interim Financial Reporting" ("IAS 34") and have been prepared following the same accounting policies and method of computation as the annual Financial Statements for the year ended June 30, 2012. The disclosures provided below are incremental to those included with the annual Financial Statements. Certain information and disclosures normally included in the notes to the annual Financial Statements have been condensed or have been disclosed on an annual basis only. Accordingly, these condensed interim financial statements should be read in conjunction with the annual Financial Statements for the year ended June 30, 2012, which have been prepared in accordance with IFRS as issued by the IASB.

These financial statements were reviewed by the Audit Committee and approved and authorized for issue by the Board of Directors on February 28, 2013.

(b) Basis of Consolidation

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

	Country of incorporation	Ownership - December 31, 2011	Ownership - June 30, 2012
Global CO2 Reduction Inc. ("Global CO2")	Canada	100%	100%
CO2 Reduction Poland Sp. z. o. o. ("CO2 Reduction")	Poland	100%	100%
MicroCoal Inc. ("MicroCoal")	USA	58.21%	58.21%
Carbiopel - ESP S.A.	Poland	100%	100%
MicroCoal International Inc. ("MicroCoal Canada")	Canada	100%	100%

(in Canadian dollars)

3. GOING CONCERN ISSUES

These condensed interim financial statements have been prepared using IFRS applicable to a going concern, which contemplates the realization of assets and settlement of liabilities in the normal course of business as they become due. The continuation of the Company as a going concern is dependent upon the ability of the Company to obtain necessary financing (through debt, equity or sale or assets) to fund its future development capital requirements and thereby achieve a profitable level of operations through finding and developing reserves and optimizing future production. These material uncertainties lend doubt as to the ability of the Company to meet its obligations as they come due and, accordingly, the appropriateness of the use of accounting principles applicable to a going concern.

The Company incurred a loss of $2,396,025 (year ended June 30, 2012: $4,735,380) for the six months ended December 31, 2012, and had an accumulated deficit of $15,142,280 at December 31, 2012 which has been funded primarily by the issuance of equity. These factors raise doubt about the Company's ability to continue as a going concern.

These condensed interim financial statements do not reflect the 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 Company were unable to realize its assets and settle its liabilities as a going concern in the normal course of operations. Such adjustments could be material.

4. CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS

The Company makes estimates and assumptions about the future that affect the reported amounts of assets and liabilities. Estimates and judgments are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. In preparing these financial statements, the Company makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods.

The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are the determination of the carrying value of property, plant and equipment; coal technology and plant prototype, intangible assets and goodwill, the determination of income tax and share-based payments.

5. SUPPLEMENTAL CASH FLOW INFORMATION

	Six months ended December 31, 2012	Six months ended December 31, 2011
Interest paid	$ -	$ -
Income taxes paid	$ -	$ -
Value of stock options exercised	$ -	$ -
Issuance of shares for investment in Carbiopel (note 11)	$ -	$ 108,000

(in Canadian dollars)

6. COAL TECHNOLOGY AND PLANT PROTOTYPE

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 share 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 and cash equivalents	$ 10,036
Property, plant and equipment	29,632
Coal technology	7,059,324
Accounts payable and accrued liabilities	(842,680)
Loans payable	(2,585,521)
Fair value	3,670,791
Non-controlling interest	(1,534,024)
Consideration (10,957,778 common shares)	$ 2,136,767

In addition to the Share Exchange, the Company was to complete a private placement financing of up to $6 million (the "Financing") and from such proceeds, the Company was to pay (i) US$1 million cash to Orica, 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 would own 100% of MicroCoal. This transaction did not occur prior to the agreed closing date, September 30, 2011, however, the Company has arranged a purchase of the remaining 41.79% interest in MicroCoal. The Company paid the sum of $225,000 USD which has been recorded as a reduction of loans payable. Subsequent to December 31, 2012, the Company completed the acquisition, see note 22.

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.

The asset is being amortized on a straight-line basis over a period of 5 years commencing when the asset is available for use. As of December 31, 2012, the accumulated amortization was $2,353,803 (June 30, 2012 - $2,000,837).

	December 31, 2012	June 30, 2012
Coal technology and plant prototype	$ 7,059,324	$ 7,059,324
Accumulated amortization	$ (2,706,768)	(2,000,837)
	$ 4,352,556	$ 5,058,487

7. RECEIVABLES

	December 31, 2012	June 30, 2012
GST/HST/VAT recoverable	$ 71,773	$ 136,531
Trade receivables	19,444	93,287
	$ 91,217	$ 229,818

(in Canadian dollars)

8. PROPERTY AND EQUIPMENT

Property and equipment	Computer equipment	Equipment	Automotive equipment	Leasehold improvements	Total
July 1, 2011	$ 35,412	$ 73,769	$ -	$ 8,614	$ 117,795
Additions	-	496,930	85,329	-	582,259
Disposals	-	-	(2,829)	-	(2,829)
Effect of foreign exchange	(452)	(32,074)	(6,673)	-	(39,199)
June 30, 2012	34,960	538,625	75,827	8,614	658,026
Additions	-	-	7,440	-	7,440
Disposals	(12,564)	(54,077)	-	-	(66,641)
Effect of foreign exchange	476	40,627	7,110	-	48,213
December 31, 2012	$ 22,872	$ 525,175	$ 90,377	$ 8,614	$ 647,038
Accumulated amortization					
July 1, 2011	$ 23,766	$ 40,189	$ -	$ 3,692	$ 67,647
Acquisitions	-	125,108	27,675	-	152,783
Disposals	-	-	(471)	-	(471)
Amortization	3,365	22,035	5,840	984	32,224
Effect of foreign exchange	(456)	(8,380)	(3,656)	-	(12,492)
June 30, 2012	26,675	178,952	29,388	4,676	239,691
Acquisitions	-	-	-	-	-
Disposals	(7,353)	(34,811)	(471)	-	(42,635)
Amortization	488	23,898	7,082	394	31,862
Effect of foreign exchange	578	12,539	3,976	-	17,093
December 31, 2012	20,388	180,578	39,975	5,070	246,011
Net book value, June 30, 2012	$ 8,285	$ 359,673	$ 46,439	$ 3,938	$ 418,335
Net book value, December 31, 2012	$ 2,484	$ 344,597	$ 50,402	$ 3,544	$ 401,027

9. DEPOSIT

The deposit represents an amount paid in advance for the lease of office premises. See also note 18, commitments.

(in Canadian dollars)

10. ACQUISITION OF CARBIOPEL - ESP S.A.

Pursuant to the original and amended agreements, on February 20, 2012 a total of 1,967,000 shares of the Company were issued with a fair value of $531,090 to acquire 100% ownership of Carbiopel Eco Stream Power S.A. ("Carbiopel"). Carbiopel is a biomass pellet producer based out of Poland that focuses on aggregating biomass, particularly from agricultural residue, to use as feedstock for the Pellet Producing machinery. The common shares were subject to a four month holding period. The Company also agreed to lend up to $312,000 to Carbiopel at an interest rate of 4% per annum repayable on or before February 28, 2013.

The value of the Carbon Friendly shares issued was calculated using the closing share price as at the date of acquisition. The acquisition was accounted for as a business combination and the aggregate fair values of assets acquired and liabilities assumed were as follows on acquisition date:

Cash	$	7,172
Amounts receivable		8,738
Prepaids		1,032
Property, plant and equipment		432,239
Accounts payable and accrued liabilities		(54,507)
Loan from parent		(112,000)
Fair value		282,674
Consideration (1,967,000 common shares)		531,090
Goodwill	$	248,416

The acquired amounts receivables are classified as loans and receivables and consist primarily of VAT receivable. It is expected that the full amount will be recovered.

Incurred in connection with this acquisition was an immaterial amount of transaction costs, which were expensed during the year ended June 30, 2012.

The goodwill was attributable mainly to the skills and technical talent of Carbiopel's work force and the synergies expected to be achieved from integration of Polish operations. Subsequent to the date of acquisition, management has estimated the synergies effect did not materialize as expected and the amount of $248,416 has been written off as of June 30, 2012.

11. INTANGIBLE ASSETS

	December 31, 2012	June 30, 2012
Exclusive sales contract (i)	$ 108,383	$ 104,695
Impairment charge (i)	(104,018)	(55,121)
	$ 4,365	$ 49,574

(i) Exclusive Sales Contract

As of December 31, 2012, the Company reviewed the carrying amount of its intangible assets and recognized an impairment charge of $49,574 in the consolidated statements of comprehensive loss (June 30, 2012 - $Nil).

During the years 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. The Company has not acquired additional rights to sell carbon credits during the current year. As of December 31, 2012, the Company has 1,512,364 (June 30, 2012 — 1,500,000) verified emission reduction credits.

(in Canadian dollars)

12. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

	December 31, 2012	June 30, 2012
Trade accounts payable	$ 772,518	$ 680,728
Accrued interest on loans	29,649	18,557
Taxes and payroll deductions	14,204	5,549
Debt subject to cancellation on completion of acquisition of MicroCoal, Inc.	1,362,129	1,326,544
	$ 2,178,500	$ 2,031,378

13. LOANS PAYABLE

	December 31, 2012	June 30, 2012
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, 2012 the Company repaid $160,000 (2011 - $202,000). The remaining balance of $100,000 was due in January 2012. The Company is negotiating with the lender to extend the loan and the amount has been classified as current liability.	$ 100,000	$ 100,000
Pursuant to a loan agreement, a total of $48,000 was advanced to the Company on an unsecured basis. A 20% loan bonus was charged with the loan amount calculated at $60,000 to be repaid. The interest rate is 10% per annum and the principal was due at the earlier of September 12, 2012 or if a financing was achieved by the Company. The Company is negotiating with the lender to extend the terms of the loan and the amount has been classified as current liability.	1,500	60,000
Pursuant to a loan agreement a total of $125,000 was advanced to the Company. The interest rate is at 10% per annum. The loan was payable on or before March 23, 2012. The Company is negotiating with the lender to extend the terms of the loan and the amount has been classified as current liability.	115,000	115,000
Pursuant to a loan agreement a total of $30,000 was advanced to the Company. The interest rate is at 18% per annum. A loan placement fee of $6,000 and legal fees of $562 are payable. The loan is payable within 60 days after demand. This amount has been classified as current liability.	36,562	-
Pursuant to a loan agreement a total of 30,000 zloty was advanced to the Company. The interest rate is at 20% per annum. The loan is payable upon demand. This amount has been classified as current liability.	9,785	-
Pursuant to a loan agreement dated June 2, 2008, MicroCoal received $2,250,000 USD 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 6), 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. As the acquisition for the remaining interest has not completed, the provision has not in effective as of June 30, 2012. The Company is negotiating with the terms of the repayment.	2,018,433	2,178,370
	$ 2,281,280	$ 2,453,370

(in Canadian dollars)

14. SHARE CAPITAL

(a) Authorized: unlimited common shares without par value

(b) **Issued and Outstanding**

Six months ended December 31, 2012

On December 28, 2012 the Company closed non-brokered private placement of 8,673,750 units at a price of $0.20 per Unit, for gross proceeds of $1,734,750. Each unit is comprised of one common share of the Company and one common share purchase warrant. Each warrant entitles the holder thereof to purchase one common share of the Company at an exercise price of $0.35 per common share until December 28, 2014. Finders' fees of $26,750 were paid and 1,244,250 finder's warrants were issued on the same terms as the Unit warrants. The fair value of the broker's warrants of $115,829 was estimated using the Black-Scholes option pricing model using a risk free interest rate of 1.11%, an expected dividend yield of $nil, a volatility of 118% and an expected life of warrants of 2 years.

Year ended June 30, 2012

On February 13, 2012 a private placement was completed consisting of 6,395,766 units at $0.30 per unit, each unit consisting of one common share and one share purchase warrant. Each warrant entitles the holder to purchase one common share of the Company at an exercise price of $0.45 per common share for a period of two years from the closing date of the private placement. The Company paid share issuance costs of $118,587 related to legal and professional fees and issued 297,909 broker warrants. The fair value of the broker's warrants of $35,990 was estimated using the Black-Scholes option pricing model using a risk free interest rate of 1.11%, an expected dividend yield of $nil, a volatility of 88% and an expected life of warrants of 2 years. The broker warrants have the same exercise price and terms as for the private placement units.

On October 19, 2011 a private placement was completed consisting of 5,495,000 units at $0.20 per unit, each unit consisting of one common share and one share purchase warrant. Each warrant entitles the holder to purchase one common share of the Company at an exercise price of $0.35 per share for a period of two years. The Company paid share issuance costs of $29,900 related to legal and professional fees and issued 509,313 broker warrants. The fair value of the broker's warrants of $47,410 was estimated using the Black-Scholes option pricing model using a risk free interest rate of 0.91%, an expected dividend yield of $Nil, a volatility of 118% and an expected life of warrants of 2 years. The broker warrants have the same exercise price and terms as for the private placement units.

c) **Warrants**

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

	Number of shares		Exercise Price
Balance, June 30, 2011	15,020,450		0.41
Issued	12,697,988		0.40
Expired	(7,675,200)		0.35
Balance, June 30, 2012	20,043,238		0.42
Issued	9,918,000		0.35
Expired	(2,072,500)		0.75
Balance, December 31, 2012	27,888,738	$	0.37

The following table summarizes warrants outstanding and exercisable at December 31, 2012:

Warrants Outstanding	**Warrants Exercisable**	**Exercise Price**	**Expiry Date**
5,272,750	5,272,750	$0.35	June 30, 2013
6,004,313	6,004,313	$0.35	September 30, 2013
6,693,675	6,693,675	$0.45	February 13, 2014
9,918,000	9,918,000	$0.35	December 28, 2014
27,888,738	27,888,738		

(in Canadian dollars)

14. SHARE CAPITAL continued

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, 2011	3,831,620		0.24
Granted	1,420,000		0.22
Expired	(261,620)		0.25
Outstanding, June 30, 2012	4,990,000		0.23
Granted	1,750,000		0.10
Exercised	(200,000)		0.14
Cancelled	(710,000)		0.23
Outstanding, December 31, 2012	5,830,000	$	0.20

During the period ended December 31, 2012, the Company granted 1,080,000 options at an exercise price of $0.11, 670,000 options at a price of $0.09 and 885,000 options at a price of $0.335 to officers, directors and consultants. The options vested immediately.

The following table summarizes stock options outstanding and exercisable at December 31, 2012:

Options Outstanding	Exercise Price	Expiry Date	Options Exercisable
590,000	$0.14	August 18, 2016	590,000
1,600,000	$0.20	February 8, 2016	1,600,000
805,000	$0.23	October 6, 2013	805,000
675,000	$0.36	December 16, 2014	675,000
410,000	$0.32	December 22, 2016	410,000
1,080,000	$0.11	August 18, 2016	1,080,000
670,000	$0.09	October 12, 2016	670,000
5,830,000			5,830,000

During the period ended December 31, 2012, share-based compensation has been recorded in the amount of $212,122 and included in share-based payment reserve. The weighted average life of the options is 3.11 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:

	Six months ended December 31, 2012	**Year ended June 30, 2012**
Risk free interest rate	**1.25%**	**1.25%**
Expected dividend yield	**nil%**	**nil%**
Stock price volatility	**103.0%**	**97.8%**
Expected life of options	**3.11**	**3.11**

(in Canadian dollars)

14. SHARE CAPITAL continued

e) Share-based payment reserve

	Six months ended December 31, 2012	Year ended June 30, 2012
Balance, beginning of period	$ 1,743,317	$ 1,404,017
Stock-based compensation	212,122	255,900
Fair value of agent's warrants	-	83,400
Balance, end of period	$ 1,955,439	$ 1,743,317

15. RELATED PARTIES

Key management includes the Chief Executive Officer, the President and the Chief Financial Officer. Compensation paid or payable to key management for services provided during the periods ended December 31, 2012 and 2011 was as follows:

Key management personnel remuneration	**Six months ended December 31, 2012**	Six months ended December 31, 2011
Management and professional fees	$ **211,993**	$ 185,234
Automobile allowance (travel and promotion)	**14,400**	14,400
Stock-based compensation	-	85,836
Total key management personnel remuneration	$ **226,393**	$ 285,470

The Company incurred the following transactions with companies that are controlled by directors and/or officers of the Company. The transactions were measured at the exchange amount which approximates fair value, being the amount established and agreed to by the parties.

Management and directors' fees	$ **288,732**	$ 276,864
Consulting	**63,000**	$ 12,800
Automobile allowance (travel and promotion)	**14,400**	19,650
Professional fees	**54,000**	45,700
Total related party amounts	$ **420,132**	$ 355,014

As at December 31, 2012 accounts payable and accrued liabilities included $328,330 (June 30, 2012 - $354,817) owing to officers and directors. The amounts due are unsecured, non-interest bearing and have no fixed terms of repayment.

16. INCOME TAXES

As at June 30, 2012, the Company has accumulated non-capital losses of approximately $7.789 million (2011: $5.933) for Canadian income tax purposes that may be carried forward to reduce taxable income derived in future years, which expire in various amounts from 2027 to 2032. The Company also has operating losses of approximately $1,086,000 (2011: $231,000) in the United States which expire up to 2032. For Polish tax purposes, there is approximately $1.1 million operating losses which have not been included in the deferred tax assets above due to the uncertainty of the inclusion of these losses. The Company evaluates its deferred tax assets 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 unrecognized deferred tax assets are reflected in current income.

(in Canadian dollars)

17. SEGMENTED INFORMATION

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

Property and Equipment	December 31, 2012	June 30, 2012
Canada	$ 21,920	$ 16,552
USA	27,120	24,477
Poland	348,674	377,306
	$ 397,714	$ 418,335
Intangible Assets		
Canada	$ -	$ -
USA	-	-
Poland	-	46,574
	$ -	$ 46,574
Coal technology and plant prototype		
Canada	$ -	$ -
USA	4,705,521	5,058,487
Poland	-	-
	$ 4,705,521	$ 5,058,487

18. COMMITMENTS AND CONTINGENCIES

(a) The Company entered into a management agreement for a period of 3 years commencing July 1, 2011 and will pay management fees of $183,795 per year. 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 a management agreement for a period of 3 years commencing July 1, 2011 and will pay management fees of $84,000 per year. There is an annual increase of 5% per annum. In an event of a change in control, and the officer is terminated within 18 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) two year's compensation.'

(c) The Company entered into a consulting agreement for a period of 3 years commencing April 1, 2012 and will pay consulting fees of $66,000 per year. There is an annual increase of 5% per annum. In an event of a change in control, and the consultant is terminated within 12 months of such change of control, then the consultant 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.

(d) The Company entered into a consulting agreement for a period of 3 years commencing February 1, 2011 and will pay consulting fees of $168,000 per year. There is an annual increase of 5% per annum. In an event of a change in control, and the consultant is terminated within 12 months of such change of control, then the consultant 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.

(e) The Company entered into an agreement to lease additional office space as follows:

2013	47,463
2014	94,923
2015	96,266
2016	98,057
2017	24,626
	$ 361,335

18. COMMITMENTS AND CONTINGENCIES continued

(f) In prior years, the Company has acquired the 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 $104,695 for these exclusive sales contract rights and has right to sell carbon credits into the market place. If sales are found through a carbon credit certification process, further amounts would be paid to the vendors of up to 8,222,251 PLN (approximately $2.4 million) within 30 days subject to obtaining carbon credit certification or sale of a carbon credit unit from the lands.

(g) The Company is currently involved in dispute with an investor relations company who claims that the Company agreed, pursuant to an agreement, to pay a finder's fee in connection with the acquisition of MicroCoal. A formal lawsuit has been filed by the investor relations company and the fees claimed are $450,000. The amount has not been recorded as uncertainties existed related to whether claims will be settled out of court and if not whether the Company will be successful in defending any action.

19. 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.

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

20. FINANCIAL INSTRUMENTS AND RISKS

As at December 31, 2012, 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.

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

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations. The Company is mainly exposed to credit risk from credit sales and cash with major financial institutions. It is the Company's policy, implemented locally, to assess the credit risk of new customers before entering contracts. Such credit ratings are taken into account by local business practices.

(in Canadian dollars)

20. FINANCIAL INSTRUMENTS AND RISKS continued

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	
	December 31, 2012	June 30, 2012	December 31, 2012	June 30, 2012
Cash	$ -	$ 8,428	$ 4,848	$ 1,216
Receivables	-	-		95,217
Accounts payable and accrued liabilities	(274,573)	(1,774,971)	(125,851)	(65,380)
Related parties	(174,956)	(176,338)	(26,208)	(20,293)
Loans payable	(2,118,433)	(2,178,370)	-	-
	$ (2,567,962)	$ (4,121,251)	$ (147,211)	$ 10,760

The following exchange rates were applied:

	Six months ended December 31, 2012		Year ended June 30, 2012	
	Average rate	Spot rate	Average rate	Spot rate
Canadian dollars to US dollars	1.0064	1.0031	0.9969	0.9755
Canadian dollars to Zloty	3.2511	3.0858	3.1675	3.3584

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. There are various objections and political risks in relation to the carbon credit market place.

21. EVENTS OCCURING AFTER REPORTING DATE

On January 7, 2013 the Company announced it concluded its agreement with Orica US Services Inc. ("Orica") and acquired 100% ownership of MCI (note 6). Orica transferred all remaining shares to MCI, and all Orica directors and management resigned from the MCI Board of Directors. Pursuant to agreements signed on December 5, 2012, May 17, 2012, December 22, 2011, January 10, 2011 and October 15, 2010 (the "Agreements"), the Company agreed to pay the sum of $1 million (USD) to Orica of which $225,000 has been paid, leaving a balance of $775,000 bearing interest at a rate of 5% per annum. The Company has consigned 200,000 ISO 14064-2 Validated Voluntary Emission Reductions generated from the Northern Poland Afforestation Offset Project ("VERS") to Orica as security, the sale of which can reduce the debt. With the acquisition of MicroCoal being concluded, various debts and loans originally in the books of MicroCoal are forgiven as per the Agreements resulting in a recovery of $2.6 million. This amount will be reported as income in the 3rd quarter financial statements.

The Company issued 1,777,777 shares to management and aconsultant as recompensement for efforts made as approved by the board of directors and the CNSX Exchange.

The Company announced a non-brokered private placement of up to 5,000,000 units at a price of $1.00 per unit, for gross proceeds of up to$5,000,000. Each unit is comprised of one common share of the Company and one common share purchase warrant. Each warrant entitles the holder to purchase one common share of the Company at a price $1.25 each for a period of two years from the closing date.

The Company granted incentive stock options to directors, officers and consultants of the Company to purchase 885,000 common shares in the capital stock of the Company exercisable on or before January 7, 2017 at an exercise price of $0.335 per share.