



**CarbonEnergy**

**ABN 56 057 552 137**

**AND CONTROLLED ENTITIES**

**HALF YEAR FINANCIAL REPORT**  
**DECEMBER 2008**

**CARBON ENERGY LIMITED  
ABN 56 057 552 137  
AND CONTROLLED ENTITIES**

*Incorporated under the Corporations Act 2001 in the State of Western Australia on 29th September 1992.*

**HALF YEAR FINANCIAL REPORT  
FOR THE PERIOD ENDED 31 DECEMBER 2008**

**CORPORATE DETAILS**

**Directors:**

|  |   |                    |
|--|---|--------------------|
| K. Robinson B.Sc.(Geology)             | - | Chairman           |
| A.M Dash BE(Chem), MCom                | - | Managing Director  |
| C.W. Mallett MSc, PhD, FAIE            | - | Technical Director |
| I.W. Walker B.Sc. Hons.(Geology)       | - | Director           |
| M.D.J. Cozijn B. Com. ASA MAICD.       | - | Director           |
| P.T. McIntyre B.Sc (Eng), MBA, FIEAust | - | Director           |
| J.G. Linley PhD, B.Sc. Hons.           | - | Director           |
| P.N. Hogan B.Bus, ACA.                 | - | Director           |

**Secretary:**

P.K. Nair B Bus (Acctg), MBA, FCA, FCIS, FTIA, MAICD

**Registered & Principal Office:**

Level 12, 301 Coronation Drive  
MILTON QLD 4064  
Telephone: + 617 3337 9944  
Facsimile: +617 3337 9945

**Postal Address:**

PO Box 2118  
TOOWONG DC QLD 4066

**Share Registry Perth:**

Security Transfer Registrars Pty Ltd  
770 Canning Highway  
APPLECROSS WA 6153

**Solicitors Perth:**

Deacons  
Level 39, Bank West Tower  
108 St George's Terrace  
PERTH WA 6000

**Auditors:**

WHK Horwath  
Level 6, 256 St Georges Terrace  
PERTH WA 6000

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**CARBON ENERGY LIMITED**  
**ABN 56 057 552 137**

**HALF YEAR DECEMBER 2008 FINANCIAL REPORT**

**DIRECTORS' REPORT**

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Your Directors submit the financial report of the economic entity for the half year ended 31 December 2008, made in accordance with a resolution of the Board.

***DIRECTORS***

The names of directors who held office during or since the end of the half year:

Mr Kim Robinson  
Mr Andrew Dash  
Dr Cliff Mallett  
Mr Ian Walker  
Mr Max Cozijn  
Mr Peter McIntyre  
Dr Shad Linley (appointed 15 July 2008)  
Mr Peter Hogan (appointed 29 August 2008)

***REVIEW OF OPERATIONS***

The economic entity incurred a loss after income tax of \$7,156,716 for the half year which included significant expenses of \$5,272,952 as outlined in note 3 (2007: loss \$1,858,845 with no significant expenses).

The Company has achieved the following highlights during this half year:

|                                      |
|--------------------------------------|
| <b>HIGHLIGHTS FOR THE SIX MONTHS</b> |
|--------------------------------------|

◆ **BLOODWOOD CREEK UCG TRIAL (Carbon Energy 100%)**

- During the period, Carbon Energy successfully constructed and commissioned its Underground Coal Gasification (UCG) project at Bloodwood Creek in Queensland, applying its world leading UCG technology and commenced a 100 day trial.
- The trial period was completed on 3 February 2009 having achieved a world first for UCG production by producing commercial quantities of gas based on oxygen and steam injection. Key outcomes from the trial included:
  - ◆ Demonstration of sustained production of air injected syngas suitable for low cost generation of power (achieved in November 2008);
  - ◆ Demonstration of production of high value oxygen injected syngas suitable for the production of low emission electricity, chemicals and liquid fuels;
  - ◆ The conversion of un-mineable coal in-situ to gas energy at an average rate of 20PJ per million tonnes in the Surat basin;
  - ◆ Validation of Carbon Energy's proprietary design and economic models which can be applied to any suitable coal seam anywhere in the world; and
  - ◆ Consistently achieving, and exceeding, target energy content and flow rates.

- In January 2009 Carbon Energy announced an increase in its coal resources. The Bloodwood Creek deposit has a JORC (2004) compliant Indicated and Inferred coal resource to which a 5m and 2m thickness cut-off has been applied as follows:

| Location                                 | Coal Seam Thickness | Indicated (Mt) | Inferred (Mt) | TOTAL (Mt) |
|--|---------------------|----------------|---------------|------------|
| Bloodwood Creek<br>(MDL 374 and EPC 867) | 2                   | 211.7          | 85.2          | 296.9      |
|  | 5                   | 109.7          | 35.2          | 144.9      |

- In February 2009 the Queensland Government announced a new policy in relation to UCG and Coal Seam Gas (CSG) tenements which provides Carbon Energy with exclusive rights to the resource contained within its MDL 374. Approximately 75% of 224 million tonnes of Carbon Energy's resource is contained within MDL 374. This represents 4,480 PJ of energy in situ of which 2,500 PJ is potentially recoverable as UCG syngas.
- In January 2009 a 517 hectare freehold property was acquired adjacent to the Bloodwood Creek site providing the ideal location for industrial projects utilising Carbon Energy's coal resources.
- Letter of Intent executed with LyondellBasell during the period for the formation of a working group to progress a pre feasibility study into the production of methanol.

#### ◆ URANIUM (Carbon Energy 100%)

- At Nyang, significant Uranium mineralisation has been delineated over a strike length of more than 3km within a palaeochannel extending at least 11km.

## CORPORATE

- Consistent with its strategy, Carbon Energy has completed its restructure of the Management team and relocation of Registered Office to Brisbane effective January 2009 which included:
  - ◆ Effective as from 1 January 2009, Mr Andrew Dash has been appointed Chief Executive Officer and Managing Director, Mr Prem Nair has been appointed Chief Financial Officer and Company Secretary, and Mr Peter Swaddle appointed General Manager – Commercial, with Carbon Energy founders, Dr Cliff Mallett and Mr Rusty Mark continuing as Technical Director UCG and Business Development Manager, respectively
  - ◆ Founding Carbon Energy Limited Shareholders and Directors, Mr Ian Walker and Mr Max Cozijn remain as non-executive directors of the Company, having previously held the roles of Managing Director and Finance Director, respectively.

### Issued Capital

- The total issued capital at 31 December 2008 was 491,296,637 fully paid ordinary shares quoted on the Australian Stock Exchange. Additionally, a total of 75,000,000 unlisted options with exercise prices between 15c and \$1.60c (with vesting dates ranging between 30 June 2009 and 30 June 2012, with the majority also subject to meeting of annual key performance indicators (KPIs) and performance hurdles being met) are on issue.
- During the period, the Company issued 2,000,000 unlisted Options with an exercise price of \$0.60 to Southern Cross Equities as part of the consideration for raising capital for Carbon Energy. These Options expire at 30 June 2011.
- A total of 7,407,408 shares remain to be issued to Dr Cliff Mallett and Mr Rusty Mark upon the successful completion of the Bloodwood Creek Trial and associated analysis of trial results.

## Listed Investments

- Carbon Energy holds 10 million shares in ASX listed nickel-copper-platinum group metals (PGE) explorer Magma Metals Limited. Magma is actively exploring in Canada and Western Australia.

## Funds on Hand

- As at 31 December 2008 funds on hand were \$9 million with a further \$2.9 million available in equity investments.

## Auditors Independence Declaration

The lead auditor's independence declaration under section 307C of the Corporation Act 2001 is set out on page 5 for the half-year ended 31 December 2008.

*This report is signed in accordance with a resolution of the Board of Directors.*



**K. Robinson**  
Chairman



**A.M. Dash**  
Managing Director

Dated this 5<sup>th</sup> day of March 2009

## Competent Person Statement – Coal

*The information in this release that relates to resources is based on information compiled by Dr C.W. Mallett, Executive Director Carbon Energy Limited who is a member of the Australian Institute of Mining and Metallurgy. Dr Mallett has sufficient experience which is relevant to the style of mineralization and type of deposit under consideration and to the activity which he is undertaking to qualify as a Competent Person as defined in the 2004 Edition of the "Australasian Code for Reporting of Exploration Results, Mineral Resources and Ore Reserves". Dr Mallett consents to the inclusion in the release of the matters based on his information in the form and context in which it appears.*

## Competent Person Statement – Gold and Uranium

*The information in this report that relates to Exploration Results, Mineral Resources or Ore Reserves is based on information compiled by Mr I.W. Walker, Non-Executive Director of Carbon Energy Limited who is a member of the Australian Institute of Geoscientists. Mr Walker has sufficient experience which is relevant to the style of mineralisation and type of deposit under consideration and to the activity which he is undertaking to qualify as a Competent Person as defined in the 2004 Edition of the "Australasian Code for Reporting of Exploration Results, Mineral Resources and Ore Reserves". Mr Walker consents to the inclusion in the report of the matters based on their information in the form and context in which it appears.*

#### AUDITOR'S INDEPENDENCE DECLARATION

In accordance with the requirements of section 307C of the Corporations Act 2001, as lead auditor for the review of Carbon Energy Ltd for the half-year ended 31 December 2008, I declare that, to the best of my knowledge and belief, there have been:

- a) no contraventions of the auditor independence requirements of the Corporations Act 2001 in relation to the review; and
- b) no contraventions of any applicable code of professional conduct in relation to the review.

WHK HORWATH PERTH AUDIT PARTNERSHIP



CYRUS PATELL  
Principal

Perth, WA

Dated this 5<sup>th</sup> day of March 2009

**CARBON ENERGY LIMITED**  
**ABN 56 057 552 137**  
**AND CONTROLLED ENTITIES**

**CONSOLIDATED INCOME STATEMENT**  
**FOR THE HALF YEAR ENDED 31 DECEMBER 2008**

|  | Notes | ECONOMIC ENTITY           |                           |
|--|-------|---------------------------|---------------------------|
|  |       | 31 December<br>2008<br>\$ | 31 December<br>2007<br>\$ |
| Revenues   |       | 699,855                   | 441,291                   |
| Employee benefits expense                                  |       | (589,361)                 | (313,096)                 |
| Depreciation expense                                       |       | (24,951)                  | (10,681)                  |
| Administration costs                                       |       | (1,020,403)               | (451,685)                 |
| Consultancy costs  |       | (99,904)                  | (146,652)                 |
| Exploration expenditure                                    |       | (408,507)                 | (553,782)                 |
| Tenement holding costs                                     |       | (141,701)                 | (137,908)                 |
| Other expenses   |       | (298,792)                 | (126,816)                 |
| Share-based payments                                       | 2 & 3 | (1,480,602)               | -                         |
| Unrealised loss on revaluation of investments              | 3     | (2,744,000)               | -                         |
| Restructuring - Redundancies                               | 3     | (1,048,350)               | -                         |
| Share of net losses of joint venture entities              |       | -                         | (559,516)                 |
| Profit/(Loss) before income tax expense                    |       | (7,156,716)               | (1,858,845)               |
| Income tax expense   |       | -                         | -                         |
| Profit/(Loss) attributable to members of the parent entity |       | (7,156,716)               | (1,858,845)               |
| <b>Overall Operations:</b>                                 |       |                           |                           |
| Basic earnings/(Loss) per share (cents per share)          |       | (1.46)                    | (0.72)                    |
| Diluted earnings/(Loss) per share (cents per share)        |       | (1.46)                    | (0.72)                    |

*The accompanying notes form part of these financial statements*

**CARBON ENERGY LIMITED**  
**ABN 56 057 552 137**  
**AND CONTROLLED ENTITIES**

**CONSOLIDATED BALANCE SHEET**  
**AS AT 31 DECEMBER 2008**

|   | <b>ECONOMIC ENTITY</b>      |                         |
|---|-----------------------------|-------------------------|
|   | <b>31 December<br/>2008</b> | <b>30 June<br/>2008</b> |
|   | <b>\$</b>                   | <b>\$</b>               |
| <b>CURRENT ASSETS</b>                     |                             |                         |
| Cash and cash equivalents                 | 8,988,560                   | 25,651,820              |
| Trade and other receivables               | 520,227                     | 629,581                 |
| Financial assets                          | 2,941,535                   | 5,685,535               |
| <b>TOTAL CURRENT ASSETS</b>               | <b>12,450,322</b>           | <b>31,966,936</b>       |
| <b>NON CURRENT ASSETS</b>                 |                             |                         |
| Trade and other receivables               | 430,134                     | 382,477                 |
| Property, plant & equipment               | 21,995,956                  | 7,933,309               |
| Deferred exploration and evaluation costs | 95,694,584                  | 95,222,555              |
| Intangible assets                         | 2,499,999                   | 2,499,999               |
| <b>TOTAL NON CURRENT ASSETS</b>           | <b>120,620,673</b>          | <b>106,038,340</b>      |
| <b>TOTAL ASSETS</b>                       | <b>133,070,995</b>          | <b>138,005,276</b>      |
| <b>CURRENT LIABILITIES</b>                |                             |                         |
| Trade and other payables                  | 1,847,742                   | 879,852                 |
| Short-term provisions                     | 39,317                      | 249,374                 |
| <b>TOTAL CURRENT LIABILITIES</b>          | <b>1,887,059</b>            | <b>1,129,226</b>        |
| <b>TOTAL LIABILITIES</b>                  | <b>1,887,059</b>            | <b>1,129,226</b>        |
| <b>NET ASSETS</b>                         | <b>131,183,936</b>          | <b>136,876,050</b>      |
| <b>EQUITY</b>                             |                             |                         |
| Issued capital                            | 150,927,675                 | 151,126,952             |
| Reserves                                  | 1,835,671                   | 171,792                 |
| Accumulated losses                        | (21,579,410)                | (14,422,694)            |
| <b>TOTAL EQUITY</b>                       | <b>131,183,936</b>          | <b>136,876,050</b>      |

*The accompanying notes form part of these financial statements*



**CARBON ENERGY LIMITED  
ABN 56 057 552 137  
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**CONSOLIDATED STATEMENT OF CHANGES IN EQUITY  
FOR THE HALF YEAR ENDED 31 DECEMBER 2008**

|   | <b>ECONOMIC ENTITY</b>  |                             |                         |                    |
|---|-------------------------|-----------------------------|-------------------------|--------------------|
|   | Issued<br>Capital<br>\$ | Accumulated<br>Losses<br>\$ | Option<br>Reserve<br>\$ | Total<br>\$        |
| <b>Balance at 1 July 2007</b>   | 26,113,727              | (12,410,648)                | 137,646                 | 13,840,725         |
| Shares issued during the period   | 5,678,169               | -                           | -                       | 5,678,169          |
| Movement in share option reserve  | -                       | -                           | 38,747                  | 38,747             |
| Losses attributable to members of parent entity                         | -                       | (1,858,845)                 | -                       | (1,858,845)        |
| <b>Balance at 31 December 2007</b>                                      | <b>31,791,896</b>       | <b>(14,269,493)</b>         | <b>176,393</b>          | <b>17,698,796</b>  |
| <b>Balance at 1 July 2008</b>   | 151,126,952             | (14,422,694)                | 171,792                 | 136,876,050        |
| Shares issued during the period   | 247,000                 | -                           | -                       | 247,000            |
| Transaction costs   | (449,342)               | -                           | 408,342                 | (41,000)           |
| Exercise of options   | 3,065                   | -                           | (3065)                  | -                  |
| Movement in share option reserve on recognition of share based payments | -                       | -                           | 1,258,602               | 1,258,602          |
| Losses attributable to members of parent entity                         | -                       | (7,156,716)                 | -                       | (7,156,716)        |
| <b>Balance at 31 December 2008</b>                                      | <b>150,927,675</b>      | <b>(21,579,410)</b>         | <b>1,835,671</b>        | <b>131,183,936</b> |

*The accompanying notes form part of these financial statements*

**CARBON ENERGY LIMITED  
ABN 56 057 552 137  
AND CONTROLLED ENTITIES**

**CONSOLIDATED CASH FLOW STATEMENT  
FOR THE HALF YEAR ENDED 31 DECEMBER 2008**

|   | <b>ECONOMIC ENTITY</b>             |                                    |
|---|------------------------------------|------------------------------------|
|   | <b>31 December<br/>2008<br/>\$</b> | <b>31 December<br/>2007<br/>\$</b> |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES</b>               |                                    |                                    |
| Payments to suppliers and employees                       | (2,250,564)                        | (710,539)                          |
| BWC Trial construction and operations                     | (14,007,546)                       | -                                  |
| Payments for exploration and development expenditure      | (934,032)                          | (633,610)                          |
| Interest received   | 639,017                            | 62,942                             |
| Administration services                                   | 18,053                             | 43,750                             |
| Other receipts  | 47,568                             | -                                  |
| R&D tax concession refunds received                       | -                                  | 36,907                             |
| Net cash used in operating activities                     | <b>(16,487,504)</b>                | <b>(1,200,550)</b>                 |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES</b>               |                                    |                                    |
| Payments for property, plant and equipment                | (119,599)                          | (1,025)                            |
| Proceeds from sale of property, plant & equipment         | 5,000                              | -                                  |
| Investment in unlisted entity                             | -                                  | (1,650,000)                        |
| Investments in term deposits – performance bonds          | (45,157)                           | -                                  |
| Proceeds from sale of investments                         | -                                  | 17,172                             |
| Net cash flows provided by (used in) investing activities | <b>(159,756)</b>                   | <b>(1,633,853)</b>                 |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES</b>               |                                    |                                    |
| Proceeds from issues of shares                            | 25,000                             | 6,000,000                          |
| Capital raising costs                                     | (41,000)                           | (321,831)                          |
| Net cash flows provided by financing activities           | <b>(16,000)</b>                    | <b>5,678,169</b>                   |
| Net increase (decrease) in cash held                      | <b>(16,663,260)</b>                | <b>2,843,766</b>                   |
| Cash at 1 July 2008                                       | <b>25,651,820</b>                  | <b>1,796,915</b>                   |
| Cash at 31 December 2008                                  | <b>8,988,560</b>                   | <b>4,640,681</b>                   |

*The accompanying notes form part of these financial statements*

**CARBON ENERGY LIMITED**  
**ABN 56 057 552 137**  
**AND CONTROLLED ENTITIES**

**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE HALF YEAR ENDED 31 DECEMBER 2008**

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**NOTE 1 - BASIS OF PREPARATION**

The half-year consolidated financial statement is a general purpose financial report prepared in accordance with the requirements of the Corporations Act 2001, Australian Accounting Standard AASB 134: Interim Financial Reporting, Australian Accounting Interpretations and other authoritative pronouncements of the Australian Accounting Standards Board.

It is recommended that this financial report be read in conjunction with the annual financial report for the year ended 30 June 2008 and any public announcements made by Carbon Energy Limited and its controlled entities during the half-year in accordance with continuous disclosure requirements arising under the Corporations Act 2001.

The accounting policies and methods of computation adopted in the preparation of the half-year financial report are consistent with those adopted and disclosed in the company's 2008 annual report for the financial year ended 30 June 2008.

The half-year financial report does not include full disclosures of the type normally included in an annual financial report and therefore cannot be expected to provide as full an understanding of the financial performance, financial position and financing activities of the consolidated entity as the full financial report.

**Reporting Basis and Conventions**

The half-year report has been prepared on an accruals basis and is based on historical costs modified, by the revaluation of selected non-current assets, financial assets and financial liabilities for which fair value basis of accounting has been applied.

**NOTE 2 – SHARE-BASED PAYMENTS**

The following share based payments arrangements existed at 31 December 2008.

On 3 July 2008, 2,000,000 Share Options were granted to Southern Cross Equities for services in relation to capital raisings. These Options have an exercise price of \$0.60 and expire on 30 June 2011.

On 14 August 2008 600,000 fully paid shares were issued to employees. On the date of issue, the share price was \$0.37 per share, valuing the shares at \$222,000.

On 16 September 2008, 10,500,000 Share Options were granted to employees as follows:

| <u>No. of Options</u> | <u>Exercise Price</u> | <u>Vesting date*</u> | <u>Expiry date</u> |
|-----------------------|-----------------------|----------------------|--------------------|
| 3,500,000             | \$0.80                | 30/06/2009           | 10/12/2013         |
| 3,500,000             | \$1.20                | 30/06/2010           | 10/12/2013         |
| 3,500,000             | \$1.60                | 30/06/2011           | 10/12/2013         |

On 17 October 2008, 6,000,000 Share Options were granted to employees as follows:

| <u>No. of Options</u> | <u>Exercise Price</u> | <u>Vesting date*</u> | <u>Expiry date</u> |
|-----------------------|-----------------------|----------------------|--------------------|
| 2,000,000             | \$0.80                | 31/10/2009           | 10/12/2013         |
| 2,000,000             | \$1.20                | 31/10/2010           | 10/12/2013         |
| 2,000,000             | \$1.60                | 31/10/2011           | 10/12/2013         |

**CARBON ENERGY LIMITED  
ABN 56 057 552 137  
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**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE HALF YEAR ENDED 31 DECEMBER 2008**

**NOTE 2 - SHARE-BASED PAYMENTS (Continued)**

On 13 November 2008 pursuant to Shareholder approval 35,250,000 Share Options were granted to executive directors as follows:

| <u>No. of Options</u> | <u>Exercise Price</u> | <u>Vesting date*</u> | <u>Expiry date</u> |
|-----------------------|-----------------------|----------------------|--------------------|
| 5,000,000             | \$0.25                | 30/06/2009           | 10/12/2013         |
| 7,000,000             | \$0.35                | 30/06/2010           | 10/12/2013         |
| 8,000,000             | \$0.70                | 30/06/2011           | 10/12/2013         |
| 10,000,000            | \$1.00                | 30/06/2012           | 10/12/2014         |
| 1,750,000             | \$0.80                | 30/06/2009           | 10/12/2013         |
| 1,750,000             | \$1.20                | 30/06/2010           | 10/12/2013         |
| 1,750,000             | \$1.60                | 30/06/2011           | 10/12/2013         |

\*Vesting is conditional upon continuity of service and achievement of Performance Benchmarks.

All Options granted are for Ordinary Shares in Carbon Energy Limited, which confer a right of one ordinary share for every Option held.

None of the Options hold voting or dividend rights. If the Option holder ceases to be in the employment of the company prior to vesting, the Options will lapse.

|  | <u>No. of Options</u> | <u>Exercise Price</u> |
|--|-----------------------|-----------------------|
| Outstanding at the beginning of the period | 21,500,000            | \$0.17                |
| Granted                                    |                       |                       |
| 3 July 2008                                | 2,000,000             | \$0.60                |
| 16 September 2008                          | 3,500,000             | \$0.80                |
|  | 3,500,000             | \$1.20                |
|  | 3,500,000             | \$1.60                |
| 17 October 2008                            | 2,000,000             | \$0.80                |
|  | 2,000,000             | \$1.20                |
|  | 2,000,000             | \$1.60                |
| 13 November 2008                           | 5,000,000             | \$0.25                |
|  | 7,000,000             | \$0.35                |
|  | 8,000,000             | \$0.70                |
|  | 10,000,000            | \$1.00                |
|  | 1,750,000             | \$0.80                |
|  | 1,750,000             | \$1.20                |
|  | 1,750,000             | \$1.60                |
| Exercised                                  | (250,000)             | \$0.10                |
| Outstanding at period end                  | <u>75,000,000</u>     | <u>\$0.67</u>         |
| Exercisable at period end                  | <u>23,500,000</u>     | <u>\$0.21</u>         |

The weighted average fair value of the Options granted during the period was \$0.15. This price was calculated using a Black Sholes Option Pricing Model applying the following inputs:

**CARBON ENERGY LIMITED  
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**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE HALF YEAR ENDED 31 DECEMBER 2008**

**NOTE 2 - SHARE-BASED PAYMENTS (Continued)**

|                                 |            |
|---------------------------------|------------|
| Weighted average exercise price | \$0.87     |
| Weighted average life of option | 5.04 years |
| Underlying share price          | \$0.37     |
| Expected share price volatility | 70%        |
| Risk free interest rate         | 5.25%      |

**NOTE 3 – PROFIT / LOSS FOR THE PERIOD**

The following significant revenue and expense items are relevant in explaining the financial performance:

|  | <b>31 Dec.<br/>2008 \$</b> | <b>31 Dec.<br/>2007 \$</b> |
|--|----------------------------|----------------------------|
| <b>Share based payments</b>  | (1,480,602)                | -                          |
| This expense relates to accounting for share options provided to employees in accordance with the Australian Accounting Standards and are based on a theoretical cost using a 70% volatility factor. |                            |                            |
| <b>Unrealised loss on revaluation of investments</b>   | (2,744,000)                | -                          |
| This expense relates to “marking” the MMB investment to Market (i.e. the MMB share price at 31 December 2008).   |                            |                            |
| <b>Restructuring – Redundancies</b>  | (1,048,350)                | -                          |
| This expense relates to focussing on the syngas operations in Queensland and moving the registered office to Brisbane which has resulted in the Perth based positions becoming redundant.            |                            |                            |

**NOTE 4 – CONTINGENT LIABILITIES**

There has been no material change in contingent liabilities since the last annual reporting date other than:

**Capital Expenditure Commitments**

As at 30 June 2008 the company had capital expenditure commitments of \$14,535,000 relating to the Bloodwood Creek Trial construction. At 31 December 2008 this commitment had reduced to \$1,900,000.

In addition, up to a maximum of 15 million fully paid Carbon Energy Limited shares are to be issued to Constellation Energy, subject to completion of documentation, associated with directional drill holes for the UCG panel.

**NOTE 5 – EVENTS SUBSEQUENT TO REPORTING DATE**

The Company has acquired a 517 hectare freehold property adjacent to the Bloodwood Creek site in January 2009 for \$385,000 which will provide the ideal location for industrial projects utilising Carbon Energy’s coal resources.

On 18<sup>th</sup> February 2009, the Queensland Government announced a new policy in relation to overlapping tenements between UCG and CSG producers that clarifies the issue of priority access to resources and provides a clear pathway for all parties to move to production. The key outcome for Carbon Energy is that the policy provides priority and certainty of tenure for the Company for the resource contained within its existing Mineral Development Licence area (MDL 374).

No other matters or circumstances have arisen since the end of the financial period, which significantly affected or may significantly affect the operations of the economic entity, the results of those operations, or the state of the affairs for the economic entity in subsequent financial years.

**CARBON ENERGY LIMITED**  
**ABN 56 057 552 137**

**DIRECTORS' DECLARATION**

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The directors of the company declare that:

- (a) The financial statements and notes, as set out on pages 6 to 13:
  - (i) comply with Accounting Standard AASB134: Interim Financial Reporting and the Corporations Regulations 2001; and
  - (ii) give a true and fair view of the economic entity's financial position as at 31 December 2008 and of its performance for the half year ended on that date.
- (b) In the directors' opinion there are reasonable grounds to believe that the company will be able to pay its debts as and when they become due and payable.

This declaration is made in accordance with a resolution of the Board of Directors:



**K. Robinson**  
Chairman



**A.M. Dash**  
Managing Director

Brisbane, Queensland  
5<sup>th</sup> March 2009

**INDEPENDENT AUDITOR'S REVIEW REPORT  
TO THE MEMBERS OF CARBON ENERGY LTD AND ITS CONTROLLED ENTITIES**

**REPORT ON THE HALF-YEAR FINANCIAL REPORT**

We have reviewed the accompanying half-year financial report of Carbon Energy Ltd and its Controlled Entities (the consolidated entity), which comprises the balance sheet as at 31 December 2008, and the income statement, statement of changes in equity and cash flow statement for the half-year ended on that date, statement of accounting policies, other selected explanatory notes and the directors' declaration.

**Directors' responsibility for the half-year financial report**

The directors of the consolidated entity are responsible for the preparation and fair presentation of the half-year financial report in accordance with Australian Accounting Standards (including the Australian Accounting Interpretations) and the Corporations Act 2001. This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and fair presentation of the half-year financial report that is free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

**Auditor's responsibility**

Our responsibility is to express a conclusion on the half-year financial report based on our review. We conducted our review in accordance with the Auditing Standard on Review Engagements ASRE 2410: *Review of an Interim Financial Report Performed by the Independent Auditor of the Entity*, in order to state whether, on the basis of the procedures described, we have become aware of any matter that makes us believe that the financial report is not in accordance with the Corporations Act 2001 including giving a true and fair view of the consolidated entity's financial position as at 31 December 2008 and its performance for the half-year ended on that date; and complying with the Accounting Standard AASB 134: Interim Financial Reporting and the Corporations Regulations 2001. As the auditor of Carbon Energy Ltd and its Controlled Entities, ASRE 2410 requires that we comply with the ethical requirements relevant to the audit of the annual financial report.

A review of a half-year financial report consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with Australian Auditing Standards and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

**Independence**

In conducting our review, we complied with the independence requirements of the Corporations Act 2001.

**Conclusion**

Based on our review, which is not an audit, we have not become aware of any matter that makes us believe that the half-year financial report of Carbon Energy Ltd and its Controlled Entities is not in accordance with the Corporations Act 2001, including:

- a) giving a true and fair view of the consolidated entity's financial position as at 31 December 2008 and of its performance for the half-year ended on that date; and
- b) complying with Accounting Standard AASB 134: Interim Financial Reporting and Corporations Regulations 2001.

WHK HORWATH PERTH AUDIT PARTNERSHIP



CYRUS PATELL  
Principal

Perth, WA  
Dated this 5<sup>th</sup> day of March 2009