



Quarterly Report

June 2010

Corporate Details

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

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

Quarterly Report For the period ended 30 June 2010

CURRENT DIRECTORS:

K. Robinson BSc (Geology) – Chairman
A.M Dash BEng (Chem), MCom - Managing Director
C.W. Mallett MSc, PhD, FAIE - Technical Director
M.D.J. Cozijn B Com, ASA, MAICD - Director
P.N. Hogan B.Bus, ACA – Director
L.I. Rozman BEng, MGeos, FAusIMM CP(Man), MAICD (appointed 7 Apr. 2010)
I.W. Walker BSc Hons (Geology) - Director

SECRETARY:

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

MANAGEMENT TEAM:

A Dash - Managing Director
C Mallett - Technical Director
J Bidwell – General Manager Project Development
A Mifflin – General Manager Technical Services
P Nair – CFO & Company Secretary
P Swaddle – General Manager – Commercial

REGISTERED & PRINCIPAL OFFICE:

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SHARE REGISTRY:

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SOLICITORS:

Gadens Lawyers
240 Queen Street
BRISBANE QLD 4001

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Highlights

- The Panel 2 & Panel 3 drilling program commenced in late May, the work is progressing as planned.
- The Company retains cash reserves of \$19.07 million as at 30 June 2010.
- The Company has negotiated an option to commence the drilling of Panel 3 immediately after the completion of Panel 2.
- Pacific Road Capital completed its acquisition of a 10% interest in CNX from the CSIRO.
- Pacific Road Capital introduced one of their significant international investment fund shareholders in the Pacific Road Resources Fund to take a direct interest of 4.9% in CNX, with the Pacific Road Resources Fund holding the balance of 5.1%. As previously announced, the transaction was undertaken at \$0.60 per share.
- Commissioning of the 5 MW project will now be completed utilising gas from the planned second UCG panel, anticipated to be completed by August/September 2010.

Energy – Underground Coal Gasification

- Carbon Energy Ltd (CEL) is an emerging energy Company intent on producing syngas for cleaner energy and chemical feedstock from Underground Coal Gasification (UCG). It aims to do this by pursuing the following key areas of focus:

Continuous improvement of UCG technology and the development of complementary technologies that will ensure CNX will develop a superior technical capability in the UCG Syngas industry.

Expand its coal resource inventory by exploration within its current tenements or through identification of suitable joint venture opportunities and acquisitions, leveraged off CEL's ability to successfully undertake UCG Syngas production in Australia and globally.

Identify and develop commercial opportunities using Syngas derived from Carbon Energy's superior UCG technology for the production of power, synthetic natural gas, chemicals and gas to liquids (GTL) either in the Company's own right or by way of strategic partnerships.

Progress in each of these key areas is as follows:

1. CONTINUOUS IMPROVEMENT OF UCG TECHNOLOGY (BLOODWOOD CREEK)

Further developments on the Bloodwood Creek site are continuing as follows:

As per the company's announcement dated 28th April commissioning of the 5 MW project will be completed in September, in line with the availability of the gas from Panel 2



5MW Plant construction in progress

- The drilling program for Panel 2 & 3 commenced in late May, the work is progressing as planned. Some of the key features of the progress achieved to the end of June being as follows:
 - Drilling of vertical injection wells for panels 2&3 completed and seam position confirmed
 - First 70 meters of both the product and injection wells for panel 2 have been drilled cased and grouted



Vertical drilling rig for drilling of Panel 2

- All major items of equipment have been procured and Panel 2 ignition and gas gathering items installed
- The ignition well installation design has been improved.
- Panel 1 has continued to operate at a reduced output capacity whilst considering the panel remediation protocol.
- Close coordination with the Queensland Government's working parties associated with the Government's UCG Policy continues.

20MW Power Station Development

The proposed 20MW power station is now configured as a steam turbine following initial review of engineering advice and discussions with prospective commercial partners. Proposals for a FEED (Front

End Engineering Design) Study have been received and are being reviewed with selection of our preferred engineering partner to occur in the near future.



Proposed 20MW Power Station Site

2. EXPAND COAL RESOURCE

- **Chile**

Carbon Energy and Antofagasta are working closely together on site selection at Mulpun, Chile for the development of the Company's first international UCG project.

Phase 1: activities, which include a work plan and budget for the trial and associated activities such as site selection and seismic evaluation, are progressing well. Further work will be undertaken in Chile by Carbon Energy's Technical and Project Team in late July. Design parameters for the initial trial will be finalised following completion of the site assessment, with the commencement of the trial likely in the first quarter of 2011.

- **Galilee Basin (QLD)**

Discussions are ongoing with Liberty Resources in order to formalise a joint venture agreement that will earn Carbon Energy an 80% interest in Liberty's granted EPC's in the Galilee Basin by Carbon Energy funding the early stages of underground development through to a trial project.

- **Other opportunities**

Carbon Energy continues in discussions to identify other potential coal resources suitable for UCG both in Australia and Internationally.

Tenement Status at end June 2010

| Tenement | Status | Sub-blocks as at March 2010 | Sub-blocks as at June 2010 | Area Sq km |
|--------------------|-------------|-----------------------------|----------------------------|------------|
| MLA 50253 | Application | 1342 ha | 1342 ha | 15 |
| MDL 374 | Granted | 2687 ha | 2687 ha | 32 |
| 867 | Granted | 191 | 191 | 670 |
| 869 | Granted | 64 | 64 | 213 |
| 868 | Granted | 177 | 177 | 605 |
| 1132 | Granted | 23 | 23 | 78 |
| 1109 | Granted | 65 | 65 | 224 |
| 1741 Kogan West | Application | 35 | 35 | 119 |
| | | | TOTAL | 1,956 |

3. IDENTIFY AND DEVELOP COMMERCIAL OPPORTUNITIES

Commercial negotiations are continuing with a short-list of partners to develop Carbon Energy's planned 20-25MW power project in Queensland, the selection of a preferred partner is targeted now for late 2010. An assessment of market opportunities for Carbon Energy's proposed 300 MW power project at the Company's 'Blue Gum Energy Park' will be made in due course.

Discussions are continuing with resource owners in North America and Europe regarding Carbon Energy earning an equity position in coal resources suitable for UCG by providing access to the Company's leading UCG technology.

Corporate

BOARD CHANGES

- Louis Rozman, a Director of Pacific Road Capital, was appointed to the Board at the start of the Quarter.

SUBSTANTIAL SHAREHOLDERS

- Pacific Road announced in May 2010 that it had completed its acquisition of a 10% interest in the Company from CSIRO. Pacific Road Capital has introduced one of their significant international investment fund shareholders in the Pacific Road Resources Fund to take a direct interest of 4.9% in CNX and Pacific Road Resources Fund holding the balance of 5.1%. The transaction was completed at \$0.60 per share, with Pacific Road Capital holding an option over CSIRO's remaining 4.8% interest in CNX at a price of \$0.93 per share.
- Incitec Pivot Limited has notified their holding in the CNX as 11.3%
- Lujeta Pty Ltd notified their holding in CNX as 5%.

ISSUED CAPITAL & CASH FUNDS

- The total issued capital at the end of the Quarter was 609,497,650 fully paid ordinary shares quoted on the Australian Stock Exchange. During the quarter 15,000,000 New Shares were issued to Constellation Energy Pty Ltd in consideration for the supply of drilling services by Constellation for the Bloodwood Creek Trial.
- A total of 49,921,000 unlisted options with exercise prices between 20c and \$1.60 are on issue (with expiry dates ranging between 31 October 2010 and 22 March 2015, with the vast majority subject to meeting annual performance measures). 2,139,000 options lapsed during the Quarter.
- The Company retains cash reserves of \$19.07 million as at 30 June 2010.

LISTED INVESTMENTS

- Carbon Energy held 29 million shares in ASX listed uranium company, Energia Minerals Limited as at 30 June 2010

For and on behalf of the Board



A.M. Dash
Managing Director
27 July 2010

Coal Resource Summary – Appendix A

As at 30th June 2010

March 2010 Quarter Resource Statement

| Location | Seam Thickness Cut-Off | Indicated (Mt) | Inferred (Mt) | TOTAL (Mt) |
|-----------------|---------------------------|-------------------|------------------|---------------|
| Bloodwood Creek | 2 | 218 | 280 | 498 |
| | 5 ¹ | 158 | 57 | 215 |
| Kogan | 2 | | 170 | 170 |
| | 5 ¹ | | 149 | 149 |
| Total Resource | 2 | 218 | 450 | 668 |
| | 5 ¹ | 158 | 206 | 364 |

Notes:

1. Optimal target for Underground Coal Gasification

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.

In accordance with Society of Petroleum Engineers (SPE) guidelines, the reserves in these properties are:

| AREA | CATEGORY | GROSS GAS VOLUMES(PJ) |
|--|---|-----------------------|
| Bloodwood Creek EPC 867 (including MDL 374) | 1P Reserve (Proven) | 11 |
| | 2P Reserve (Proven + Probable) | 743 |
| | 3P Reserve (Proven + Probable + Possible) | 1,042 |

The reserve estimates used in this document were compiled by Mr Timothy Hower of MHA Petroleum consultants, Colorado, USA, a qualified person under ASX Listing Rule 5.11. Mr Hower has consented to the use of the reserve information contained within this document in the form and context in which it appears.

Appendix 5B

Mining exploration entity quarterly report

Introduced 1/7/96. Origin: Appendix 8. Amended 1/7/97, 1/7/98, 30/9/2001.

Name of entity

CARBON ENERGY LIMITED

ABN

ABN 56 057 552 137

Quarter ended ("current quarter")

30 JUNE 2010

Consolidated statement of cash flows

| Cash flows related to operating activities | | Current Quarter \$A'000 | Year to Date (12 months) \$A'000 |
|---|---|----------------------------|--|
| 1.1 | Receipts from product sales and related debtors | - | - |
| 1.2 | Payments for (a) exploration and evaluation (net) | - | (233) |
| | (b) development – BWC Operations | (2,479) | (8,639) |
| | (c) technical services | (721) | (1,403) |
| | (d) administration (net) | (1,125) | (3,020) |
| | (e) commercial and business devel. | (486) | (1,502) |
| 1.3 | Dividends received | - | - |
| 1.4 | Interest and other items of a similar nature received | 378 | 718 |
| 1.5 | Interest and other costs of finance paid | - | - |
| 1.6 | Income taxes benefit received | - | - |
| 1.7 | Other (provide details if material) Fuel tax credits | - | 173 |
| | Net Operating Cash Flows | (4,433) | (13,906) |
| Cash flows related to investing activities | | | |
| 1.8 | Payment for purchases of: (a) prospects | - | - |
| | (b) equity investments | - | - |
| | (c) other fixed assets | - | (321) |
| 1.9 | Proceeds from sale of: (a) prospects | - | - |
| | (b) equity investments | - | - |
| | MMW Shares | - | 6,464 |
| | (c) other Gold tenements & fixed assets sales | 1,500 | 2,541 |
| 1.10 | Loans to other entities | - | - |
| 1.11 | Loans repaid by other entities | - | - |
| 1.12 | Other (provide details if material) – Construction of 5MW Plant, 2 nd & 3 rd UCG Panels, Site Infrastructure, Water Monitoring wells and 20MW Plant | (5,282) | (14,876) |
| | Net investing cash flows | (3,782) | (6,192) |
| 1.13 | Total operating and investing cash flows (carried forward) | (8,215) | (20,098) |

+ See chapter 19 for defined terms.

Appendix 5B
Mining exploration entity quarterly report

| | Current Quarter \$A'000 | Year to Date (12 months) \$A'000 |
|---|----------------------------|--|
| 1.13 Total operating and investing cash flows (brought forward) | (8,215) | (20,098) |
| Cash flows related to financing activities | | |
| 1.14 Proceeds from issues of shares, options, etc. | 800 | 13,511 |
| 1.15 Proceeds from sale of forfeited shares | - | - |
| 1.16 Proceeds from borrowings | - | - |
| 1.17 Repayment of borrowings | - | - |
| 1.18 Dividends paid | - | - |
| 1.19 Other – Trade Creditors/Debtors | 4,202 | 3,526 |
| Net financing cash flows | 5,002 | 17,037 |
| Net increase (decrease) in cash held | (3,213) | (3,061) |
| 1.20 Cash at beginning of quarter/year to date | 22,290 | 22,138 |
| 1.21 Exchange rate adjustments to item 1.20 | - | - |
| 1.22 Cash at end of quarter | 19,077 | 19,077 |

Payments to directors of the entity and associates of the directors

Payments to related entities of the entity and associates of the related entities

| | |
|---|----------------------------|
| | Current Quarter \$A'000 |
| 1.23 Aggregate amount of payments to the parties included in item 1.2 | 196 |
| 1.24 Aggregate amount of loans to the parties included in item 1.10 | - |
| 1.25 Explanation necessary for an understanding of the transactions | |
| <p>Costs included in item 1.23 above covers Directors' expenses for any services undertaken outside the scope of directors duties, salaries for the Brisbane based executive Directors plus Non-Executive Director's fees and superannuation.</p> | |

Non-cash financing and investing activities

- 2.1 Details of financing and investing transactions which have had a material effect on consolidated assets and liabilities but did not involve cash flows

Accrual and creditors of up to \$4.2 million (for the quarter) have been included in the actual amounts and reversed as an adjustment to ascertain the closing cash position in item 1.19 above.

- 2.2 Details of outlays made by other entities to establish or increase their share in projects in which the reporting entity has an interest

+ See chapter 19 for defined terms.

Nil

Financing facilities available

Add notes as necessary for an understanding of the position.

| | Amount available \$A'000 | Amount used \$A'000 |
|---------------------------------------|-----------------------------|------------------------|
| 3.1 Loan facilities | - | - |
| 3.2 Credit standby arrangements/bonds | 203 | 203 |

Estimated cash outflows for next quarter

| | \$A'000 |
|--------------------------------|--------------|
| 4.1 Exploration and evaluation | 0 |
| 4.2 Development | 1,800 |
| 4.3 Production | 0 |
| 4.4 Administration | 900 |
| Total | 2,700 |

Reconciliation of cash

Reconciliation of cash at the end of the quarter (as shown in the consolidated statement of cash flows) to the related items in the accounts is as follows.

| | Current quarter \$A'000 | Previous quarter \$A'000 |
|--|----------------------------|-----------------------------|
| 5.1 Cash on hand and at bank | 909 | 2,636 |
| 5.2 Deposits at call | 17,965 | 19,200 |
| 5.3 Bank overdraft | - | - |
| 5.4 Other (Deposit Bonds) | 203 | 454 |
| Total: cash at end of quarter (item 1.22) | 19,077 | 22,290 |

Changes in interests in mining tenements

| Tenement reference | Nature of interest | Interest at beginning of quarter | Interest at end of quarter |
|-----------------------|--------------------|--|----------------------------------|
|-----------------------|--------------------|--|----------------------------------|

+ See chapter 19 for defined terms.

Appendix 5B

Mining exploration entity quarterly report

| | | | | | |
|-----|---|-------------|------------------------------|------|------|
| 6.1 | Interests in mining tenements relinquished, reduced or lapsed | | | Nil | Nil |
| 6.2 | Interests in mining tenements acquired or increased | Coal | Refer Activity Report hereto | 100% | 100% |

Issued and quoted securities at end of current quarter

Description includes rate of interest and any redemption or conversion rights together with prices and dates.

| | | Total number | Number quoted | Issue price per security (cents) | Amount paid up per security (cents) |
|-----|--|--------------------|--------------------|----------------------------------|-------------------------------------|
| 7.1 | Preference securities (description) | Nil | Nil | - | - |
| 7.2 | Changes during quarter (a) Increases through issues (b) Decreases through returns of capital, buy-backs, redemptions | - | - | - | - |
| 7.3 | +Ordinary securities | 609,497,650 | 609,497,650 | Various | Fully Paid |
| 7.4 | Changes during quarter (a) Issue of shares in relation to a service contract | 15,000,000 | 15,000,000 | @20c | Fully paid |
| 7.5 | +Convertible debt securities (description) | Nil | Nil | - | - |
| 7.6 | Changes during quarter (a) Increases through issues (b) Decreases through securities matured, converted | - - | - - | - - | - - |

+ See chapter 19 for defined terms.

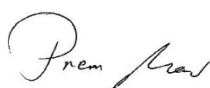
Appendix 5B
Mining exploration entity quarterly report

| 7.7 | Options | | | <i>Exercise price</i> | <i>Expiry date</i> |
|------|--|-----------------------------------|-------------|-------------------------|--|
| | Unlisted Options 20c | 250,000 | - | 20c | 31/10/2010 |
| | Unlisted Options 20c | 125,000 | - | 20c | 01/01/2011 |
| | Unlisted Options 30c | 500,000 | - | 30c | 30/06/2011 |
| | Unlisted Options 60c | 1,000,000 | - | 60c | 30/06/2011 |
| | Unlisted Options 25c | 100,000 | - | 25c | 01/04/2012 |
| | Unlisted Options 40c | 205,000 | - | 40c | 01/04/2012 |
| | Unlisted Options 25c | 5,000,000 | - | 25c | 10/12/2013 |
| | Unlisted Options 35c | 7,000,000 | - | 35c | 10/12/2013 |
| | Unlisted Options 70c | 8,000,000 | - | 70c | 10/12/2013 |
| | Unlisted Options 80c | 7,250,000 | - | 80c | 10/12/2013 |
| | Unlisted Options 80c | 1,000,000 | - | 80c | 22/03/2015 |
| | Unlisted Options \$1.00 | 10,000,000 | - | \$1.00 | 10/12/2014 |
| | Unlisted Options \$1.20 | 3,750,000 | - | \$1.20 | 10/12/2013 |
| | Unlisted Options \$1.20 | 1,000,000 | - | \$1.20 | 22/03/2015 |
| | Unlisted Options \$1.60 | 3,750,000 | - | \$1.60 | 10/12/2013 |
| | Unlisted Options \$1.60 | 1,000,000 | - | \$1.60 | 22/03/2015 |
| 7.8 | Options | | | | |
| | Issued during quarter | - | - | - | - |
| 7.9 | Exercised during quarter Unlisted Employee/Other Options | - | - | - | - |
| 7.10 | Expired during quarter Unlisted Employee Options – ceased employment | 1,000,000 1,000,000 130,000 | - - - | \$1.20 \$1.60 40c | 10/12/2003 10/12/2003 01/04/2012 |
| 7.11 | Debentures (totals only) | Nil | Nil | | |
| 7.12 | Unsecured notes (totals only) | Nil | Nil | | |

Compliance statement

- 1 This statement has been prepared under accounting policies which comply with accounting standards as defined in the Corporations Act or other standards acceptable to ASX.
- 2 This statement does give a true and fair view of the matters disclosed.

Sign here:



Date:.....27 July 2010.....

Print name: Prem Nair

Title: **Chief Financial Officer &
Company Secretary**

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+ See chapter 19 for defined terms.