

INNOVATION IN
CARBON
CAPTURE

Innovation in Carbon Capture

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Annual report 2011

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2011

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NATURE'S POWER FOR CARBON CAPTURE

Based in Quebec City, CO₂ Solution Inc. (“CO₂ Solution” or the “Company”) is a leading innovator in the field of enzyme enabled carbon capture and is actively working to validate at pilot scale and commercialize its technology for power plants and other large stationary sources of carbon pollution. In this process, CO₂ Solution has built an extensive portfolio of issued and pending patents covering the use of the enzyme, carbonic anhydrase, or analogues thereof, for post-combustion carbon capture, including the kinetic enhancement of low-energy amine, amino acids, and carbonate solutions for efficient CO₂ absorption and regeneration.

- Founded in 1997 in Quebec City, CO₂ Solution was listed on the TSX Venture Exchange (Canada) in March 2004.
- The Company's technology underwent proof-of-concept testing at the Alcoa aluminum smelter in Deschambault, Quebec and at the Quebec City waste incinerator, both of which successfully demonstrated the utility of the enzymatic platform for industrial carbon capture.
- From 2006 to 2008, CO₂ Solution worked with industrial partner Babcock & Wilcox to test its bio-technological platform under industrially relevant operating conditions. The work performed helped develop and advance the technology towards larger scale deployment.
- In 2009, the Company entered into a Joint Development Agreement (JDA) with Codexis, Inc. of Redwood City, California. Under the agreement, Codexis is developing and supplying industrially advanced carbonic anhydrase enzymes to help speed the commercial readiness of CO₂ Solution's carbon capture technology platform. The JDA was extended in January 2011.
- In December 2010, the Company entered into an exclusive Collaboration Agreement with a global leader in energy and infrastructure projects with over 5 billion dollars in annual sales, and Codexis, Inc., CO₂ Solution's exclusive enzyme development and production partner. The agreement covers the development and pilot scale testing of its carbon capture technology to reduce carbon dioxide pollution from coal-fired power plants, one of the world's largest sources of greenhouse gas emissions.
- In April 2011, the Company entered into a Collaboration Agreement with Alcoa and Codexis, Inc. for a new pilot program focused on carbon capture technology designed to sequester industrial carbon emissions, neutralizing the material to create a commercially viable product and thus reducing the environmental impact of industrial by-products.
- As of September 29, 2011, CO₂ Solution's intellectual property estate consisted of 23 issued patents (Canada, the United States and Europe) with 25 others pending.

This Annual Report may contain forward looking statements which contain the Company's current expectations about its future results. Please refer to page 6 for cautionary statements.

REPORT TO SHAREHOLDERS

Dear Shareholders,

The consensus among the scientific community, the public and our governments is quite clear; the world is getting warmer due to human activity and global warming is accelerating. The main culprit is carbon dioxide emitted from the use of fossil fuels to meet our ever increasing energy appetite; an appetite which is forecast to double by 2035. While renewables and nuclear energy will gain in prominence, their role will be marginal and fossil fuels will remain the primary energy source for decades to come. In addition, the unfortunate Japan tsunami disaster of this past March, and its devastating effect on a major Japanese nuclear power-generating facility, has thrown a question mark over nuclear energy use worldwide. Many countries are now trying to accelerate the development and implementation of technologies that clean carbon dioxide emissions from conventional fossil fuel plants, technologies such as that developed and patented by CO₂ Solution.

In this respect, 2011 was a year of strong growth and of important milestones for CO₂ Solution. It was, once again, a record setting year in terms of commercial and technical progress that built upon the very significant achievements of 2010. Additional milestones were set, and met, moving us further down the path towards commercial deployment of our unique, game-changing and patented carbon capture technology.



Fiscal 2011 Highlights

Technology Development and Validation

The impressive technical results and advancements announced in 2010 validated the potential of our technology and helped CO₂ Solution partner with two industry giants in strategically significant industrial sectors – fossil fuel power generation and metals refining – for the development and scale-up of our technology.

CARBON CAPTURE COLLABORATION WITH GLOBAL LEADER IN ENERGY INFRASTRUCTURE

In December 2010, CO₂ Solution and its enzyme supply partner, Codexis, Inc., entered into an exclusive Collaboration Agreement with a global leader (“Global Leader”) in energy infrastructure projects with over \$5 billion in annual sales, covering the

development and pilot scale testing of CO₂ Solution’s technology for coal-fired power plants, one of the largest global sources of harmful greenhouse gas emissions. Under the terms of the Agreement, CO₂ Solution, Codexis and the Global Leader are collaborating on a pilot phase program to develop and test customized carbon capture enzymes and related processes for use in power plants to reduce greenhouse gas emissions. Our Global Leader partner has funded all development activities under the collaboration.

The Collaboration Agreement and related Memorandum of Understanding included an option for the Global Leader to transition its carbon capture program to other solvent systems it is developing based on its assessment of the relative potential of the Technology for these systems and upon mutual agreement between the parties. As such, the Company announced in August 2011 that the Global Leader elected to cease work on the original

solvent system and provided CO₂ Solution and its enzyme collaborator, Codexis, Inc. with the requisite notice to redirect the work to the other solvent systems and of its intent to negotiate a separate definitive collaboration agreement for these other systems.

Based on past internal evaluations, supplemented by the recent technical findings from the Collaboration, CO₂ Solution believes this transition to the other solvent systems is a positive move which represents greater technical and economic potential for the Company.

PARTNERSHIP WITH ALCOA FOR PILOT TEST THAT TURNS CARBON EMISSIONS INTO BENEFICIAL COMMERCIAL PRODUCTS

On April 7, 2011, the Company unveiled a partnership and collaboration with aluminum producer Alcoa and CO₂ Solution’s exclusive enzyme development and production partner, Codexis, Inc., for a carbon capture technology pilot test that turns CO₂ emissions into beneficial commercial products.

The \$16.5 million project is being funded by Alcoa along with approximately \$13.5 million in funding from the U.S. Department of Energy (DOE) received from an award with the National Energy Technology Laboratory (NETL).

The collaboration is intended to devise solutions that treat and utilize a primary by-product of the aluminum manufacturing process known as alkaline clay, or bauxite residue, as well as other alkaline industrial residuals. This pilot project will test a scrubbing process that combines treated flue gas, enzymes and alkaline clay to create a mineral-rich neutralized product that could be used for environmental reclamation projects. Over 120 million tonnes of bauxite residue are produced annually by the aluminum industry worldwide. The project is emblematic of how Alcoa is leveraging its extensive R&D capabilities and utilizing game-changing technologies from companies like CO₂ Solution and Codexis to advance sustainable solutions that can have an impact beyond Alcoa’s operations.

CO₂ SOLUTION AND CODEXIS EXTEND THEIR CARBON CAPTURE JOINT DEVELOPMENT AGREEMENT

In January 2011, CO₂ Solution extended its carbon capture Joint Development Agreement (“JDA”) with Codexis, Inc., originally announced in December of 2009. Under the JDA, CO₂ Solution and Codexis collaborate on the development of customized carbonic anhydrase biocatalysts and related processes to enable the efficient capture of carbon dioxide from power plants and other large stationary emissions sources. Program results to date have shown that the combined CO₂ Solution/Codexis proprietary technologies have the potential to significantly lower the capital and operating cost barriers associated with conventional technologies to capture CO₂ from power plant effluent gases.

In August 2011, Codexis presented important technical progress at the CO₂ Capture Technology Meeting sponsored by the U.S. Department of Energy/National Energy Technology Laboratory. Codexis, supported by a grant from the DoE’s ARPA-E Recovery Act program, showed enzyme performance has been improved by about two million fold over natural forms of the carbonic anhydrase. Codexis-evolved enzymes are functional and stable in relatively inexpensive, energy efficient solvents for 24 hours at temperatures greater than 90°C.

Financial Resources

The capital required for testing CO₂ Solution’s technology at pilot and demonstration scale is quite important and largely surpasses the Company’s financing capabilities. Generally, the Company’s partnering strategy is to have its industrial partners assume all capital and operating costs associated with technology development and scale-up, in return for gaining exclusivity of the Company’s technology in their specific field. Accordingly, project revenues received by CO₂ Solution from our industrial collaborations in the power generation and aluminum sectors amounted to close to \$2 million for the year ended June 30, 2011, once again a first.

In addition, on August 31, 2011, CO₂ Solution announced the closing of a brokered private placement with aggregate gross proceeds of close to \$4.4 million.

The increased revenues generated in 2011 together with the proceeds from this private placement have strengthened the Company’s financial base and will provide the additional working capital required for continued technology development operations and the pursuit of other commercial market opportunities, notably in the cement and oil and gas sectors.

Intellectual Property

CO₂ Solution continues to hold the broadest portfolio of patents in the field of enzyme enhanced carbon capture with 23 patents issued and 25 pending. These patents not only cover the use of carbonic anhydrase with various capture solvents, but also the use of the enzyme in different reactor configurations and in key industrial sectors such as power generation and cement. The Company continued to build on this solid foundation in fiscal 2011 with the successful issuance of 3 new patents and the filing of 9 new patents.

CO₂ Solution announced in May 2011 that it had been granted Canadian patent No. 2499264 - *A PROCESS AND A PLANT FOR RECYCLING CARBON DIOXIDE EMISSIONS FROM POWER PLANTS INTO USEFUL CARBONATED SPECIES*, and Australian

patent No. 2006217575 - *AN IMPROVED CO₂ ABSORPTION SOLUTION*. Canadian patent No. 2499264, related to corresponding U.S. patent, No. 7,596,952, issued to CO₂ Solution in 2009, and other patents pending provides for exclusivity in the field of using the enzyme carbonic anhydrase for the capture of carbon dioxide from any fossil fuel power plant. The Company believes that this patent family has tremendous value for efficient carbon capture from power plants and aluminum operations.

Australian patent No. 2006217575, related to corresponding U.S. patent, No. 7,740,689 issued to CO₂ Solution in 2010 and other patents pending, provides for exclusivity in the field of using carbonic anhydrase for the capture of carbon dioxide with low-energy amine solvents. The Company believes that this patent family has very substantial value for the power generation, oil and gas production and other large carbon-intensive industries where the enzyme catalyst can enable the highly efficient capture of emissions with commercially available amine solvents such as methyldiethanolamine (MDEA).

These additional patents continue to enhance CO₂ Solution's leading patent position in the use of carbonic anhydrase for efficient carbon capture and further protect the Company's game-changing technology's position on a worldwide basis. With CO₂ Solution's portfolio of patents, the Company stands to uniquely benefit from the significant potential of this growing global market.

Government Regulations

Over the past year, certain governments have taken important leadership roles around the issue of reducing carbon emissions. A number of jurisdictions around the world have now established, or are in the process of developing, GHG cap-and-trade programs. Cap and Trade is a market-based system for managing and reducing industrial greenhouse gas (GHG) emissions.

Canadian provinces (British Columbia, Manitoba, Quebec, Ontario) are working with U.S. states (Arizona, California, New Mexico, Oregon, Washington, Utah, Montana) through the Western Climate Initiative (WCI) to design a cap-and-trade system that will support the transition to a low-carbon economy. WCI is a commitment by its member states to work together to identify, evaluate and implement policies that tackle climate change at a regional level. This work includes designing a broad-based GHG cap-and-trade system.

In this respect, the Province of Quebec, in July 2011, announced plans to establish its own cap and trade system whereby large industrial plants and other significant sources of carbon dioxide and other GHGs would be required to reduce their

emissions on an annual basis beginning January 1, 2013. Also in July 2011, the Government of Australia established a carbon tax to be levied as of July, 2012 for each tonne of carbon pollution emitted. The Australian carbon price mechanism will then transition in July, 2015 to an emissions trading scheme where the price will be determined by the market.

These recent government initiatives show that regulation of carbon dioxide pollution is gaining momentum and is now moving from speculation to fact. With our patented technology the Company looks forward to supporting worldwide efforts by industry to efficiently meet regulatory requirements for emissions reductions.

Outlook for 2012

Building on the significant accomplishments of 2011, management's prime focus in 2012 will be to advance the technology past the pilot stage in both the power generation and metals refining sectors through the collaboration and scale-up agreements with Alcoa and the Global Leader. In addition, the company will be looking to expand into additional industrial sectors, notably in the oil and gas and cement industries.

Further Advancing the Industrial Readiness of the Technology

Leveraging its internal R&D efforts, CO₂ Solution intends to continue to fully exploit its relationships with its industrial partners (Alcoa and Global Leader), Codexis, and Procede Group, to bring the best resources to bear in advancing its technology towards commercial readiness.

On the enzyme evolution and supply front, Codexis has made significant progress in increasing the industrial stability and longevity of the enzyme catalyst. In the area of enzyme delivery and management in the carbon capture process, the Company will continue to leverage its significant expertise in the area of enzyme immobilization. These efforts will assist in positioning CO₂ Solution's technology for the planned pilot and larger scale demonstrations under real-world conditions where significant quantities of robust enzyme are required.

On the process development and engineering front, the Company is on track to begin small pilot-scale testing at the Global Leader's and Alcoa's facilities in fiscal 2012. Working closely with Procede Group, process modeling and optimization of the enzyme with various capture solvents will provide a solid techno-economic basis to pursue this scale-up effort

beyond the pilot scale and towards larger scale field testing and commercial demonstrations.

Scale-up in Other Industrial Sectors

Encouraging discussions have also been held with large end-use customers in the cement and oil and gas sectors, notably the Canadian Oil Sands, who are interested in CO₂ Solution's technology as a potential solution to manage their carbon footprints. These opportunities, as with power generation and metals refining, represent the potential to work through tailored scale-up and validation programs, both in the lab and in the field, toward eventual commercial scale deployment in their operations and/or licensing to others in their respective industries.

Given the positive nature of a number of these discussions, management is confident that one additional scale-up partnership will be secured in 2012.

Government Funding for Development and Scale-Up

To further support its technology validation and scale-up efforts, CO₂ Solution has confidence that it can continue to tap into beneficial government funding programs in Canada, the U.S. and Europe, and with strategic partners. In Canada, the Company remains hopeful that the Federal Government will see the significant economic and environmental value that exists in supporting home grown, exportable carbon capture technologies such as CO₂ Solution's that have the potential to significantly reduce the current high cost of carbon capture in Canada and internationally. In Western Canada, the Alberta GHG reduction process has opened up new opportunities for joint projects to manage CO₂ emissions in the oil sands sector. CO₂ Solution is actively working on partnerships to advance our technology for use in this sector. In the U.S., in addition to the ARPA-E project with Codexis, and the U.S. Department of Energy support of the Alcoa project, CO₂ Solution will continue to pursue funding opportunities where possible for its technology, with the possibility of exploiting cross-border clean technology initiatives.

Expansion of Intellectual Property Dominance

Continuing along the trend started in 2008, the growth in industry interest in the potential of enzyme-enabled carbon capture was even more pronounced in 2010 and 2011. As the world searches for innovative solutions to lower the current cost barrier to CO₂ capture, enzymatic capture, largely pioneered by CO₂ Solution, has emerged as a focal point in its



own right. It is fortunate that the Company has a broad international patent position in the field which will allow it to both commercialize its technology and block potential competitors from entering the market.

Based upon the improvements to its process resulting from both our internal development efforts and our collaboration programs, CO₂ Solution will continue to expand its intellectual property dominance with the filing of new patents.

On behalf of the members of management and the Board of Directors, we would like to extend our sincere thanks to our employees and our partners for supporting the Company and delivering the significant achievements of the past year. We are also grateful to our investors for their continued support and confidence. CO₂ Solution continues to heighten its position as an innovator in the field of enzyme-enabled carbon capture and will continue working to develop and commercialize its game-changing technology for power plants and other large stationary sources of carbon pollution and maintain our position as a leader in the field.

Evan Price
Chairman of the
Board of Directors

Glenn R. Kelly
President and Chief
Executive Officer

MANAGEMENT'S DISCUSSION AND ANALYSIS

This management analysis of the operating results and the consolidated financial condition of CO₂ Solution, Inc. (“**CO₂ Solution**” or the “**Company**” or the “**Corporation**”) is for the periods ended June 30, 2011 and 2010. These consolidated financial statements include the accounts of the Company, its subsidiary companies and other entities, directly or indirectly controlled by the Company. This analysis should be read in conjunction with the audited consolidated financial statements and consolidated notes to the financial statements for the year ending June 30, 2011, which are prepared in accordance with Canadian generally accepted accounting principles. Unless otherwise specified, all numbers are expressed in Canadian dollars.



Forward-looking Statements

All statements in the 2011 Annual Report and this Management's Discussion and Analysis that are other than statements of historical facts are forward-looking statements which contain the Company's current expectations about its future results. Forward-looking statements involve numerous risks and uncertainties. The Company has attempted to identify any forward-looking statements by using words such as “anticipates”, “believes”, “could”, “expects”, “intends”, “may”, “should” and other similar expressions. Although the Company believes that the expectations reflected in all of its forward-looking statements are reasonable, it can give no assurance that such expectations will prove to be correct. A number of factors may affect the Company's future results and may cause those results to differ materially from those indicated in any forward-looking statements made by the Company. Other than as required by Canadian securities laws, the Company undertakes no obligation to publicly update or revise any of its forward-looking statements, whether as a result of changed circumstances, new information, future events, or for any other reason occurring after the date of this Management's Discussion and Analysis.

Statistical information and other data relating to the Company's industry included in the 2011 Annual Report and this Management's Discussion and Analysis are derived from recognized industry reports published by industry analysts, industry associations or independent consulting and data compilation organizations. Market data and industry forecasts used throughout the 2011 Annual Report and this Management's Discussion and Analysis were obtained from various publicly available sources. Although management believes that these independent sources are generally reliable, the accuracy and completeness of such information are not guaranteed and have not been independently verified.

Company Overview

CO₂ Solution is a leading developer of proprietary technologies for carbon dioxide (CO₂) capture and management. More specifically, the Company is currently focused on commercializing an enzyme-based, enabling technology for efficient CO₂ capture from fossil fuel-power plants and other large stationary emitters of CO₂.

Since its establishment, the Company has worked on developing its technology platform and assembling a broad patent portfolio. To support this effort, it has raised capital, recruited highly-qualified personnel and established strategic partnerships and alliances.

Sector and Potential Market Overview

Global warming comes with a big price tag for every country in the world. The reductions in emissions needed to stop climate change may not come cheaply, but the cost of failing to act will be much greater. New research shows that if present trends continue, the total cost of global warming will be as high as 3.6 percent of gross domestic product (GDP). Four global warming impacts alone – hurricane damage, real estate losses, energy costs, and water costs – will come with a price tag of almost \$1.9 trillion annually (in today’s dollars) by the year 2100. We know how to avert most of these damages through strong action to reduce the emissions that cause global warming. But the longer we wait, the more painful – and expensive – the consequences will be. (*Natural Resources Defense Council, The Cost of Climate Change*)¹.

The consensus among the scientific community, the public and our governments is clear; the world is getting warmer due to human activity. This warming is accelerating and it is urgent that we act now to slow and eventually reverse this trend by reducing our greenhouse gas (GHG) emissions. While during the past year there was no substantial North American legislative progress in this regard, past periods have been marked by announcements of more than US \$500 million in new governmental funding for the research and development of carbon capture technologies, namely in the United States and France, a recognition that the development of lower cost technologies, such as the Company’s, will be critical to exploiting the full GHG reduction potential of carbon capture and storage (CCS). Further, the unfortunate Japan tsunami disaster of this past March 2011, and its devastating effect on a major Japanese nuclear power generating facility, has thrown a question mark over nuclear energy use worldwide, with many countries now trying to accelerate the development of technology that cleans carbon dioxide emissions from conventional fuel plants².

Over the past year a number of Governments have taken important leadership roles around the issue of reducing carbon emissions. A number of jurisdictions around the world

have now established, or are in the process of developing, GHG cap-and-trade programs. Cap and Trade is a market-based system for managing and reducing industrial greenhouse gas (GHG) emissions. Canadian provinces (British Columbia, Manitoba, Quebec, Ontario) are working with U.S. states (Arizona, California, New Mexico, Oregon, Washington, Utah, Montana) through the Western Climate Initiative (WCI) to design a cap-and-trade system that will support the transition to a low-carbon economy and form a broader, North American approach. WCI is a commitment by four Canadian provinces and seven U.S. states to work together to identify, evaluate and implement policies that tackle climate change at a regional level. This work includes designing a broad-based GHG cap-and-trade system. In this respect, the Province of Quebec, in July 2011, announced plans to establish its own cap and trade system whereby large industrial plants and other significant sources of carbon dioxide and other GHGs would be required to reduce their emissions on an annual basis beginning January 1, 2013. Another example of a Government taking a leadership role on this important environmental issue was demonstrated in an announcement made on July 11, 2011 by the Prime Minister of Australia, where-by that country established a price for each tonne of carbon pollution emitted to be levied beginning July 1, 2012 with a price rise of a further 2.5% a year during a three year period until July 1, 2015. The Australian carbon price mechanism will then transition to an emissions trading scheme where the price will be determined by the market. These recent government initiatives show that regulation of carbon dioxide pollution is moving from speculation to fact and with CO₂ Solution’s patented technology the Company looks forward to supporting worldwide efforts by industry to efficiently meet regulatory requirements for emissions reductions.

Recent Developments

CO₂ Solution and Codexis Extend their Carbon Capture Joint Development Agreement

In January 2011, the Company announced that it had extended the carbon capture Joint Development Agreement (“JDA”) with Codexis, Inc., originally announced December 15, 2009. Under the JDA, CO₂ Solution and Codexis have collaborated on the development of customized carbonic anhydrase (“CA”) biocatalysts and related processes to enable the efficient capture of carbon dioxide from power plants and other large stationary emissions sources. Program results to date have shown that

¹ <http://www.nrdc.org/globalwarming>

² Bloomberg, Business Week, March 31, 2011

the combined CO₂ Solution / Codexis proprietary technologies have the potential to significantly lower the capital and operating cost barriers associated with conventional technologies to capture CO₂ from power plant effluent gases. The JDA has been extended until the later of June 30, 2012, or six months after the expiry of any third-party collaborations.

Carbon Capture Collaboration with Global Leader in Energy Infrastructure

The extension of the JDA with Codexis followed the December 2010 announcement of CO₂ Solution and Codexis entering into an exclusive Collaboration Agreement with a global leader in energy infrastructure projects with over \$5 billion in annual sales (the “Global Leader”), covering the development and pilot scale testing of the CO₂ Solution technology for coal-fired power plants, one of the largest global sources of harmful greenhouse gas emissions. Under the terms of the Agreement, CO₂ Solution, Codexis and this Global Leader will collaborate over a period of up to 16 months on a pilot phase program to develop and test customized carbon capture enzymes and related processes for use in power plants to reduce greenhouse gas emissions. The Global Leader will fund research activities under the collaboration, which may be expanded or amended to include other promising technologies and, if milestones are met and subject to negotiation of such an agreement between the parties, evolve into a long-term development and commercialization agreement.

CO₂ Solution Appoints a New Chief Financial Officer

On March 16, 2011, the Company announced that it had appointed Mr. Thom Skinner, CA as Senior Vice President, Finance & Chief Financial Officer. A recognized business leader and career financial executive, Mr. Skinner’s professional experience spans more than thirty years and includes senior financial executive roles in the financial services, manufacturing, pharmaceutical, life sciences and biotech sectors including extensive mergers and acquisition and capital raising work. Mr. Skinner will be responsible for financial, accounting and information technology operations as well as the Company’s investor relations activities.

Alcoa, CO₂ Solution and Codexis Unveil Partnership for Carbon Capture Technology Pilot Test that Turns Emissions into Beneficial Commercial Products

On April 7, 2011, the Company unveiled a partnership and collaboration with aluminum producer Alcoa and CO₂ Solution’s exclusive enzyme development and production partner Codexis, Inc., for a carbon capture technology pilot test that turns CO₂ emissions into beneficial commercial products.

The \$16.5 million project is the latest innovation from the world’s leading aluminum producer and will be funded by Alcoa along with approximately \$13.5 million in funding from the U.S. Department of Energy (DOE) by way of an award from the National Energy Technology Laboratory (NETL). This funding was made available by the American Recovery and Reinvestment Act (ARRA).

The collaboration is intended to devise solutions that treat and utilize a primary by-product of the aluminum manufacturing process known as alkaline clay, or bauxite residue, as well as other alkaline industrial residuals. This pilot project will test a scrubbing process that combines treated flue gas, enzymes and alkaline clay to create a mineral-rich neutralized product that could be used for environmental reclamation projects. Over 120 million tonnes of bauxite residue are produced annually by the aluminum industry worldwide³. The project is emblematic of how Alcoa is leveraging its extensive R&D capabilities and utilizing game-changing technologies from companies like CO₂ Solution and Codexis to advance sustainable solutions that can have an impact beyond Alcoa’s operations.

CO₂ Solution Granted New Patents

CO₂ Solution announced in May 2011 that it had been granted Canadian patent No. 2499264 - A PROCESS AND A PLANT FOR RECYCLING CARBON DIOXIDE EMISSIONS FROM POWER PLANTS INTO USEFUL CARBONATED SPECIES, and Australian patent No. 2006217575 - AN IMPROVED CO₂ ABSORPTION SOLUTION. Canadian patent No. 2499264, related to corresponding U.S. patent, No. 7,596,952 issued to CO₂ Solution

³ CSIRO, 2009

in 2009 and other patents pending provides for exclusivity in the field of using the enzyme carbonic anhydrase for the capture of carbon dioxide from any fossil fuel power plant. The Company believes that the patent family has significant value for efficient carbon capture from power plants and aluminum operations.

Australian patent No. 2006217575 related to corresponding U.S. patent, No. 7,740,689 issued to CO₂ Solution in 2010 and other patents pending, provides for exclusivity in the field of using carbonic anhydrase for the capture of carbon dioxide with low-energy amine solvents. The Company believes that this patent family has very substantial value for the power generation, oil & gas production and other large carbon-intensive industries where the enzyme catalyst can enable the highly efficient capture of emissions with commercially available amine solvents such as methyldiethanolamine (MDEA).

These additional patents further enhance CO₂ Solution's leading patent position in the use of carbonic anhydrase for efficient carbon capture and further protect the Company's game-changing technology position on a worldwide basis. With CO₂ Solution's portfolio of patents in place, the Company stands to uniquely benefit from the significant potential of this growing global market.

CO₂ Solution's Enzyme Development Partner Announces Important Technical Progress

In August, Codexis, Inc., CO₂ Solution's enzyme development partner presented important technical progress in its carbon capture program at the CO₂ Capture Technology Meeting being sponsored by the U.S. Department of Energy/National Energy Technology Laboratory. Codexis, supported by a grant from the DoE's ARPA-E Recovery Act program, is using its patented CodeEvolver™ directed evolution technology to develop customized carbonic anhydrase (CA) enzymes that could catalyze carbon capture under industrial conditions. Data showed CA performance has been improved by about two million fold over natural forms of the enzyme. Evolved CA enzymes are functional and stable in relatively inexpensive, energy efficient solvents for 24 hours at temperatures greater than 90°C.

Use of carbon capture solvents with fully developed enzymes is expected to substantially reduce the costs and energy requirements to capture CO₂ produced by coal-fired power plants. Codexis is jointly developing the technology with CO₂ Solution, Inc.

Update on Carbon Capture Program with Global Leader in Energy Infrastructure

On August 24, 2011, CO₂ Solution updated the status of its exclusive collaboration with a global leader in energy and infrastructure projects with over \$5 billion in annual sales (the "Global Leader") covering the development and pilot scale testing of CO₂ Solution's carbon capture technology (the "Technology") to reduce carbon dioxide pollution from coal and other fossil fired power plants, one of the world's largest sources of greenhouse gas emissions.

The Collaboration Agreement and related Memorandum of Understanding, originally announced December 3, 2010, included an option for the Global Leader to transition the carbon capture program to certain other solvent systems it is developing based on its assessment of the relative potential of the Technology for these systems and upon mutual agreement between the parties. As such, it was announced that the Global Leader elected to cease work on the original solvent system and provided CO₂ Solution and its enzyme collaborator, Codexis, Inc. with the requisite notice to redirect the work to the other solvent systems and of its intent to negotiate a separate definitive collaboration agreement for these certain other solvent systems.

Based on past internal evaluations and supplemented by the recent technical findings from the program, CO₂ Solution believes the intended transition to the other solvent systems is a positive move which represents greater technical and economic potential.

Private Placement

In July 2011, CO₂ Solution announced its intention to complete a brokered private placement for minimum gross proceeds of \$2 million.

The Corporation offered a minimum of approximately 8.7 million units at a price of \$0.23 per unit (the "Units"). Each Unit was to be comprised of one common share and one-half warrant. Each whole warrant will entitle its holder to acquire one additional common share of the Corporation at a price of \$0.28 per common share for a period of 24 months following the closing of the Offering. The Offering was made on a best-efforts basis by a syndicate of investment dealers composed of National Bank Financial Inc. and Mackie Research Capital Corporation.

On August 31, 2011, CO₂ Solution announced the closing of the previously announced brokered private placement of 18,901,700 units of the Corporation (the “Units”) at a price of \$0.23 per Unit for aggregate gross proceeds of \$4,347,391 (the “Offering”). Each Unit is comprised of one common share of the Corporation and one-half common share purchase warrant. Each whole warrant entitles its holder to acquire one additional common share of the Corporation at a price of \$0.28 per common share until 5:00 p.m. (Montreal Time) on August 31, 2013. Proceeds of the Offering will be used by the

Corporation to strengthen its financial base and provide additional working capital for continued development operations and the pursuit of other market opportunities.

The Corporation has received an advance ruling from the Ministère du Revenu du Québec confirming that the Corporation is a qualified issuing corporation for the purposes of the Québec Stock Savings Plan II (“QSSP II”) and that the common shares forming part of the Units are qualified shares for a QSSP II qualified mutual fund.

Selected Annual Information

	AS AT JUNE 30		
	2011	2010	2009
Total revenues	\$1,914,118	\$10,118	\$0
Net loss	\$1,267,553	\$2,070,444	\$1,850,995
Net loss per share	\$0.02	\$0.04	\$0.04
Total assets	\$2,912,437	\$3,765,813	\$3,193,774
Long-term liabilities	\$609,422	\$37,973	\$46,282

Revenues for 2011 totaled \$1,914,118 and were primarily generated from research and development collaborations between CO₂ Solution, Codexis, Alcoa and a global leader in energy and infrastructure projects. For 2010, revenues of \$10,118 were generated from the sale of enzymes for laboratory tests by a third party.

As at June 30, 2011, the decrease in total assets is mainly the result of a reduction in cash, due to the needs for the current operations of the Company offset partially by an increase in R&D tax credits receivable.

As at June 30, 2010, the increase in total assets was mainly due to an increase in cash following the private placement of December 2009 when the Company issued 10,000,000 shares to Codexis, Inc. for proceeds of \$2,000,000. Furthermore, a \$475,000 commitment fee was received from Codexis, Inc. upon the concurrent signature of a Joint Development Agreement.

Regarding long-term liabilities, this amount is comprised of two items. First, a \$475,000 commitment fee which was received from Codexis, Inc. upon signature of the Joint Development Agreement in 2009. This commitment fee does not bear interest and is refundable only if a “subsequent agreement” as defined in the JDA is executed with Codexis. As at June 30, 2011, there has been no “subsequent agreement” entered into with Codexis, hence the fee is not considered as refundable. Since there can be no determined refund date for this fee and given that Codexis and CO₂ Solution continue to collaborate on various projects, this fee has been reclassified as a long term liability with no known repayment date. The second amount included as a long term liability is a refundable contribution obtained from Economic Development of Canada of up to \$250,000 of which \$111,820 was received on March 31, 2011. This contribution is refundable starting January 2014 with equal annual payments representing 4% of the Company’s total income. The loan was accrued to a present value of \$97,820, using an estimated capitalization rate of 5%. The difference of \$14,000 between the present value and the principal amount of the loan is included with revenues in the statement of earnings.

Additional Information Concerning Results

	JUNE 30, 2011	JUNE 30, 2010
	\$	\$
Technology platform development:		
Salaries and fees	1,567,820	655,352
Government assistance and tax credits	(776,240)	(506,617)
Business development:		
Salaries and benefits	406,296	317,534
Professional employee fees	222,869	96,243
Stock-based compensation	43,088	19,903
Travel, representation and promotion	96,417	98,688
General and administrative expenses:		
Salaries and employee benefits	433,826	304,683
Rent, electricity, taxes and insurance	189,907	182,741
Professional fees	448,498	456,235
Stock-based compensation	97,809	66,666
Amortization of property, plant and equipment	54,967	62,785
Amortization of patents	41,612	33,576
Amortization of deferred credits	(9,456)	(9,771)
Net financial expenses:		
Financial expenses	6,940	4,347
Interest income	(13,608)	(23,524)

Operating Results

Comparison Between Financial Years Ended June 30, 2011 and June 30, 2010

REVENUES

The Company recorded revenues totalling \$1,914,118 for the year ending June 30, 2011, \$1,900,118 generated from research and development collaborations and \$14,000 from actualisation of Government aid (\$10,118 for the same period in 2010 from the sale of enzymes for laboratory testing).

COST OF PRODUCTS SOLD

The company incurred \$28,701 direct costs in fiscal 2011 (\$385 for the production of enzymes for the same period in 2010).

TECHNOLOGY PLATFORM DEVELOPMENT - R&D EXPENSES

Research and development expenditures, net of investment tax credits and government assistance, increased by \$648,420, totalling a cost of \$917,686 for the fiscal year ending June 30, 2011, compared with a cost of \$269,266 for the same period in 2010. This increase is mainly attributable to work done externally and by consultants relative to enzyme performance characterization under various industrially relevant operating conditions as well as to explore new avenues for enzyme immobilization and the hiring of additional employees

to support the Company's commitments under recently concluded collaboration agreements. These expenses are reduced by way of \$776,240 of accrued R&D tax credits and other government incentive payments for the year ended June 30, 2011 (\$506,617 in 2010).

BUSINESS DEVELOPMENT EXPENSES

Business development expenses amounted to \$769,523 for the fiscal year ended June 30, 2011, compared with \$532,983 for the same period in 2010. The main contributor to this increase pertains to professional fees associated with the negotiation of various collaboration agreements and variable (performance based) management remuneration payments of \$60,400 relative to the prior year, paid in January 2011.

GENERAL AND ADMINISTRATIVE EXPENSES

General and administrative expenses amounted to \$1,472,429 for the fiscal year ended June 30, 2011, compared with \$1,297,105 for the same period in 2010, an increase of \$175,324. The major factors that contributed to this increase were:

- The hiring of additional administrative personnel in March 2011
- Professional fees for the recruitment and hiring of personnel

- Variable (performance based) management remuneration payments of \$63,940 relative to the prior year, paid in January 2011
- A \$31,143 increase in share-based remuneration.

FINANCIAL EXPENSES AND INTEREST INCOME

Net financial expenses for the fiscal year ended June 30, 2011, resulted in revenues of \$6,668, compared with revenues of \$19,177 for the same period in 2010, representing a \$12,509 increase in financial expenses. This net increase is primarily due to a \$9,916 decrease in interest income, compared to the same period in 2010, relating to the temporary investments held during the respective periods.

LOSS FOR THE YEAR

The Company recorded a loss of \$1,267,553, or \$0.02 per share, for the fiscal year ended June 30, 2011, compared with a loss of \$2,070,444, or \$0.04 per share, for the same period in 2010, a decrease in the loss of \$802,891 or 39%. This favorable net decrease is attributed to the increased revenues referred to above.

Unaudited Quarterly Financial Information

The following tables provide a summary of certain elements of financial data regarding the Company for each of the last eight quarters:

QUARTERS ENDED				
	September 30, 2010	December 31, 2010	March 31, 2011	June 30, 2011
Revenues	\$91,212	\$243,075	\$732,224	\$847,607
Net loss	\$489,764	\$467,466	\$201,913	\$108,410
Net loss per share	\$0.01	\$0.01	\$0.00	\$0.00

QUARTERS ENDED				
	September 30, 2009	December 31, 2009	March 31, 2010	June 30, 2010
Revenues	\$0.00	\$0.00	\$10,118	\$0.00
Net loss	\$492,551	\$439,477	\$540,245	\$598,171
Net loss per share	\$0.01	\$0.01	\$0.01	\$0.01

4th Quarter of 2011

During the last quarter of 2011, the Company recorded a net loss of \$108,410, or \$0.00 per share, compared with \$598,171, or \$0.01 per share, for the same period in 2010, a \$489,761 decrease in the year over year quarterly loss.

Revenue from collaborative agreements increased in the last quarter by \$847,607 offset by increases in administrative and business development expenses in the last quarter of 2011 by \$71,506, due to the following factors:

- A \$83,991 increase in salaries and benefits;
- A \$56,648 decrease in professional fees due primarily to the work performed for the Company in 2010 by a public and government relations firm and legal fees for business development activities.
- A \$22,630 increase in Patent depreciation
- A \$10,937 decrease in Government assistance
- A \$9,031 increase in travel expense

Liquid Assets and Cash Flows

Cash and temporary investments totalled \$320,741 as at June 30, 2011, compared with \$2,382,205 as at June 30, 2010.

For the fiscal year ended June 30, 2011, cash flow required for operating activities amounted to \$1,988,146, compared with \$1,779,254 for 2010, representing an increase of \$208,892, primarily due to the variation between respective losses from one period to another and to the increases in non-cash working capital used and increased stock-based compensation.

For the fiscal year ended June 30, 2011, cash flow generated from investing activities totalled \$1,638,174, compared with \$567,051 required for the same period in 2010, a difference of \$2,205,228. This difference is mainly attributable to the following factors:

■ Temporary investments

Following a private placement concluded with Codexis, Inc. in December 2009, the Company issued 10,000,000 shares for gross proceeds of \$2,000,000. This amount was used to increase temporary investments. In fiscal 2011 these temporary investments were used for the Company's day-to-day activities.

■ Capital expenditures

For the fiscal year ended June 30, 2011, the Company capitalized \$142,080 in patent related costs compared to \$87,484 in 2010.

The cash flow generated by financing activities for the year ended June 30, 2011, amounted to \$110,905, compared with \$2,389,969 for the same period in 2010. This \$2,279,064 decrease is the result of the private placement concluded with Codexis, Inc. in December 2009. The Company issued 10,000,000 shares for gross proceeds of \$2,000,000 and the \$475,000 commitment fee received from Codexis, also in December 2009, Inc. upon signature of the Joint Development Agreement.

Liquidity and Solvency

To date, the Company has financed its operations mainly through cash flow obtained from research and development collaborations, the issuance of capital stock, tax credits and government assistance.

At June 30, 2011, the Company had \$133,113 in cash, \$187,628 in temporary investments and \$665,515 in outstanding accounts receivable for a total of \$986,256 (\$2,468,538 as at June 30, 2010).

As noted under recent developments, on August 31, 2011, CO₂ Solution announced the close of a brokered private placement offering with net proceeds of \$4,043,074. With the receipt of the proceeds from this offering, the Company believes it has sufficient funds to meet its cash requirements for the foreseeable future.

The Company's access to sufficient long-term capital depends on the ability to generate a profit in the future. This will depend in part on its ability to effectively commercialize its technology, the results of research and development activities, favourable market conditions, and to overall economic conditions. Investments in commercialization activities are used to generate income; however, it is difficult to predict exactly when this income will materialize.

As at June 30, 2011 the Company benefited from credit facilities in the form of an operating line of credit for an authorized amount of \$100,000, bearing interest at prime plus 2.25% and guaranteed by a \$60,000 certificate of deposit. As at June 30, 2011, this operating line of credit was unused. Subsequent to the year-end, in July 2011, the Company negotiated a new credit facility with a new bank. This new credit facility is in the form of an operating line of credit of \$150,000 bearing interest at prime plus 2% and is secured by a universal charge on the company's assets to a maximum of \$225,000.

Contractual Obligations

The Company is committed, under a lease agreement for its office premises expiring in February 2015, to paying a total amount of \$545,171. The payments scheduled for the next four years are, \$153,258 in 2012, \$152,209 in 2013, \$151,392 in 2014 and \$88,312 in 2015.

Information Regarding Capital Stock

As at September 29, 2011, the number of outstanding common shares, warrants and stock options is respectively 79,187,836, 11,773,969 and 4,535,840.

Related Party Transactions

During the fiscal year ended June 30, 2010, the Company recorded a \$475,000 advance from a shareholder with significant influence, bearing no interest and payable, under certain conditions (nil for the same period in 2009). Pursuant to the extension of the agreement with that shareholder in January 2011, repayment of this advance has now effectively been deferred indefinitely or until certain subsequent agreements may be negotiated between the parties. The amount outstanding has now been reclassified as a long-term debt.

Outlook 2011-2012

SCALE-UP PARTNERSHIP WITH GLOBAL LEADER IN POWER GENERATION

The fiscal year ended June 30, 2011 was another positive year of growth and of significant milestones met for CO₂ Solution as the company continued to build on its previous success. In addition to executing exclusive technology development agreements with Procede Group B.V., CLEA Technologies B.V., and Codexis, Inc., CO₂ Solution started work on the first scale-up partnership with a global leader in energy infrastructure and carbon capture technology with over \$5 billion in annual sales (the Global Leader). The Collaboration Agreement with this Global Leader covers the development and pilot scale testing of CO₂ Solution's technology for coal-fired power plants, one of the largest global sources of harmful greenhouse gas emissions. Under the terms of the Agreement, CO₂ Solution, Codexis and the Global Leader will collaborate over a period of up to 16 months on a pilot phase program to develop and test customized carbon capture enzymes and related processes for

use in power plants to reduce greenhouse gas emissions. The Global Leader has a large existing base of customers to which to deploy these improved capture processes, representing a clear path to market for CO₂ Solution's technology.

On August 24, 2011, CO₂ Solution updated the status of its exclusive collaboration with this Global Leader covering the development and pilot scale testing of CO₂ Solution's carbon capture technology (the "Technology") to reduce carbon dioxide pollution from coal and other fossil fired power plants, one of the world's largest sources of greenhouse gas emissions.

The Collaboration Agreement and related Memorandum of Understanding, originally announced December 3, 2010, included an option for the Global Leader to transition the carbon capture program to certain other solvent systems it is developing based on its assessment of the relative potential of the Technology for these systems and upon mutual agreement between the parties. As such, it was announced that the Global Leader elected to cease work on the original solvent system and provided CO₂ Solution and its enzyme collaborator, Codexis, Inc. with the requisite notice to redirect the work to the other solvent systems and of its intent to negotiate a separate definitive collaboration agreement for these certain other solvent systems.

Based on our past internal evaluations and supplemented by the recent technical findings from the program, CO₂ Solution believes the intended transition to the other solvent systems is a positive move which represents greater technical and economic potential.

SCALE-UP PARTNERSHIP WITH ALCOA

On April 7th, CO₂ Solution announced a new pilot program, in collaboration with Alcoa and Codexis, Inc. focused on carbon capture technology designed to sequester industrial carbon emissions from the aluminum manufacturing process and neutralizing the material to create a commercially viable product.

The \$16.5 million project is the latest innovation from the world's leading aluminum producer and will be funded by Alcoa along with approximately \$13.5 million in funding from the U.S. Department of Energy (DOE) received from an award with the National Energy Technology Laboratory (NETL). This funding was made available by the American Recovery and Reinvestment Act (ARRA) and this project is now underway.

The pilot program, part of Alcoa's ongoing commitment to enhance its operational sustainability, will use an innovative and proprietary induct scrubber technology to capture emissions. The collaboration is intended to devise solutions that

treat and utilize a primary byproduct of the aluminum manufacturing process known as alkaline clay, or bauxite residue, as well as other alkaline industrial residuals. This pilot project will test a scrubbing process that combines treated flue gas, enzymes and alkaline clay to create a mineral-rich neutralized product that could be used for environmental reclamation projects. The project is emblematic of how Alcoa is leveraging its extensive R&D capabilities and utilizing game-changing technologies from companies like CO₂ Solution and Codexis to advance sustainable solutions that can have an impact beyond Alcoa's operations.

Scientists and engineers from Alcoa Technical Center in Pittsburgh are leading the three-year project, which has an investigation phase that runs through December, 2011. The DOE grant was received as part of an initiative to find ways of converting captured carbon dioxide emissions from industrial sources into useful products such as fuels, plastics, cement and fertilizers.

ADDITIONAL SCALE-UP OPPORTUNITIES

Encouraging discussions have also been held with large end-use customers in the cement, and oil and gas sectors who are interested in CO₂ Solution's technology as a potential solution to manage their carbon footprints. In some cases, these customers may also have developed, or are developing; proprietary carbon capture processes suited to their specific emission sources which can be significantly enhanced by CO₂ Solution's enzymatic technology. These opportunities represent the potential to work through tailored scale-up and validation programs, both in the lab and in the field, toward eventual commercial scale deployment in their operations and/or licensing to others in their respective industries.

Given the positive nature of a number of these discussions, management is confident that one additional scale-up partnership will be secured during the balance of the 2012 fiscal year.

In addition to the above, CO₂ Solution's management team will continue to pursue a multi-pronged strategy aimed at advancing its technology development and deployment. The prime focus in the short term will be as follows:

ADVANCING THE INDUSTRIAL READINESS OF THE TECHNOLOGY

Leveraging its internal R&D focus and efforts, CO₂ Solution intends to continue to fully exploit its relationships with Codexis, Procede Group and CLEA Technologies, to bring the best resources to bear in advancing its technology towards commercial readiness. On the enzyme evolution and supply front, Codexis has, and is expected to continue to make

significant progress in increasing the industrial stability and longevity of the enzyme catalyst. This will assist in positioning CO₂ Solution's technology for pilot and larger scale demonstrations under real-world conditions where significant quantities of robust enzymes are required.

In the area of enzyme delivery and management in the carbon capture process, the Company will continue work on parallel technology paths, both with Cross Linked Enzyme Aggregates (CLEAs), and with internal development efforts which leverage the Company's significant expertise in the area of enzyme immobilization. This work is expected to enhance industrial readiness by incorporating leading-edge processes in which the enzyme is delivered to the carbon capture system as micro-sized particles possessing improved tolerance to high-process temperatures. In addition, these particles can be confined to the front-end CO₂ absorption stage (where the enzyme provides the maximum beneficial impact), without being exposed to the harsher, back-end desorption process, leading to improved system economics.

Lastly, on the process development and engineering front, the Company is on track to begin small pilot-scale testing at the Global Leader's facility, in fiscal 2012. Working closely with Procede Group, system optimization and modeling of the enzyme with various capture solvents should provide a solid techno-economic basis to pursue this scale-up effort towards larger scale field testing and commercial demonstrations.

LEVERAGING GOVERNMENT FUNDING FOR DEVELOPMENT AND SCALE-UP

To further support its technology validation and scale-up efforts, CO₂ Solution has confidence that it can continue to tap into beneficial government funding programs in Canada, the U.S. and abroad, and with strategic partners. In Canada, the Company remains hopeful that the Federal Government will see the significant economic and environmental value that exists in supporting home grown, exportable carbon capture technologies such as CO₂ Solution's that have the potential to significantly reduce the current high cost of carbon capture in Canada and internationally. In western Canada the Alberta GHG reduction process project has opened up new opportunities for joint projects to manage CO₂ emissions in the oil sands sector. CO₂ Solution is actively seeking partnerships to advance our technology for use in this sector. In the U.S., in addition to the ARPA-E project with Codexis, and the U.S. Department of Energy support of the Alcoa project, CO₂ Solution will continue to pursue funding opportunities where possible for its technology, with the possibility of exploiting cross-border clean technology initiatives.

CONTINUED EXPANSION OF INTELLECTUAL PROPERTY DOMINANCE

Continuing along the trend started in 2008, the growth in industry interest in the potential of enzyme-enabled carbon capture was even more pronounced in 2010 and 2011. As the world searches for innovative solutions to lower the current cost barrier to CO₂ capture, enzymatic capture, largely pioneered by CO₂ Solution, has emerged as a focal point in its own right. This is particularly the case south of the border, where the United States' government has recently invested millions of dollars in enzyme-related projects. It is fortunate that the Company has a broad international patent position in the field which will both allow it to commercialize its technology and block potential competitors from entering the market. In this regard, CO₂ Solution will continue to expand its intellectual property dominance with the filing of new patents.

RISK FACTORS AND UNCERTAINTIES

CO₂ Solution's activities are subject to a number of risks and uncertainties which could have an adverse impact on its business, financial position and operating results as described below. These are not the only factors that could affect the Company in the future. Other risks and uncertainties still unknown to the Company, or which it may consider negligible, could also affect the manner in which it conducts business.

- The Company's future outlook will largely depend on its ability to establish strategic alliances and license agreements to help bring its technology to market.
- To protect its intellectual property, the Company relies on a series of laws on patents and trademarks, on provisions for the protection of trade secrets and industrial secrets and on privacy protection measures. Despite the Company's efforts to retain and protect its proprietary rights, third parties may copy aspects of its technology or obtain information deemed proprietary without the Company's authorization. The Company cannot guarantee that the measures implemented to protect its proprietary rights will be sufficient.
- Although the Company has experienced managers and employees, it depends on the services of a limited number of executive officers and scientific personnel. The loss of any one key employee may have a detrimental effect on the Company's business.
- CO₂ Solution Technologies Inc. receives provincial and federal tax credits that could be affected by legislative changes or the interpretation of the legislation. In this regard, it received in 2010 a draft of notice of assessment from the Canada Revenue Agency questioning its status as a Canadian-controlled private corporation and of the corresponding R&D tax credits claimed for fiscal 2009. CO₂ Solution Technologies Inc. intends to firmly defend its position and expects to prevail (see note 19 of audited financial statements).
- Considering that market development in the field of climate change is closely linked to changes in environmental legislation for reduction of greenhouse gas emissions, CO₂ Solution's growth could be adversely impacted by a lack of concerted legislative efforts on the part of major industrialized countries.
- The Company's growth requires financial resources generated from a finite number of sources. Management negotiates financing agreements to meet the Company's present and future needs. To obtain the funds it requires, the Company must rely on investments from strategic partnerships, tax credits, government grants and equity financings. There is no guarantee that such funds will be available from these sources.
- The evolution of scientific knowledge in the area of CO₂ capture has become increasingly rapid. CO₂ Solution will have to remain competitive by continuously pursuing improvements in the performance of its technology platform, as well as new products and applications to meet the needs of the marketplace. Although it intends to act accordingly, nothing guarantees that its technology will not be rendered obsolete by competitive innovations. Increased competition could affect the future outlook for CO₂ Solution and reduce its ability to access important and continued financing.
- The market for the Company's products depends on the general economic climate situation that exists. The general economic climate is beyond the control of the Company. Economic slowdowns can lead to end-users delaying or canceling investments or projects, or reducing overall budgets, all of which could have a material adverse effect on the business, operating results and financial position of the Company.

Changes in Accounting Policies

Future Accounting Standards

INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS)

In 2009, the Canadian Accounting Standards Board confirmed that the Canadian GAAP, for publicly accountable enterprises, will be replaced by IFRS and take effect during the year 2011. IFRS use a conceptual framework similar to that of the Canadian GAAP, but are composed of important differences on the subjects of posting, evaluation, presentation and information to be supplied.

The Company will be required to use International Financial Reporting Standards (IFRS) for its interim and annual financial

statements beginning on July 1, 2011 and to provide a restated comparative statement in accordance with IFRS.

To prepare for the adoption of IFRS, the Company has developed an IFRS conversion plan. This plan consisted of four phases: Phase 1 – Preliminary diagnosis, planning and definition of the scope, Phase 2 – Detailed evaluation, Phase 3 – Definition of the required modifications, and Phase 4 – Implementation. The Company completed the first 3 phases and is significantly advanced in Phase 4. This involved a high-level review of the differences between current Canadian GAAP and IFRS allowing it to evaluate the potential consequences of the transition. No major changes were required to the Company’s information systems and internal control mechanisms.

We do not expect that there will be any material entries to our books required due to the IFRS transition.

The following table presents certain choices made by management pertaining to the Standard IFRS 1 (First-time adoption of IFRS), the other choices permitted by IFRS were not applicable or judged to be immaterial.

STANDARD	TOPIC	INTERNATIONAL STANDARDS	MANAGEMENT’S COMMENTS
IFRS 1 First-time Adoption of International Financial Reporting Standards	Deemed cost of property, plant and equipment	An entity may elect to measure an item of property, plant and equipment at the date of transition to IFRS at its fair value and use that fair value as its deemed cost at that date.	Given the type of capital assets held, the company will account for them as at the transition date at their depreciated cost in accordance with IFRS rather than at their fair value on this date. There is no financial impact at transition date due to this choice.
	Business combinations	IFRS 1 permits entities to elect not to restate business combinations which occurred prior to Transition date.	Management will make this IFRS election. There is no financial impact at transition date due to this choice.
	Stock option costs	IFRS 1 permits entities to elect not to restate grants which occurred and vested prior to Transition date.	Management will make this IFRS election. There is no financial impact at transition date due to this choice.
	Designation of financial instruments	Possibility of re-designating Financial instruments on the transition date.	Management reviewed the classification of its temporary investments and decided to maintain its prior designation after the transition. There is no financial impact at transition date due to this choice.

The following are subjects which were applicable for analysis by management relative to the IFRS transition. However, from this analysis, there were no material differences noted and consequently no material entries will be required at the transition date or for the comparative period.

STANDARD	INTERNATIONAL STANDARDS	MANAGEMENT'S COMMENTS
IFRS 2 Share-based Payments	<p>Entities must estimate at the end of each period the number of equity instruments expected to vest and revise that estimate, if necessary.</p> <p>IFRS 2 requires that allotments based on a vesting schedule be considered as multiple distinct grants and that the compensation expense be recognized distinctly for each part of the grant.</p>	<p>Historical information by employee class was collected to support estimates of future vesting and integrated in our calculations. At the date of transition, CO₂ Solution determined that there was no significant financial impact.</p>
IAS 16 Property, Plant and Equipment Revaluation model	<p>Parts of an item must be depreciated separately, each over the length of its useful life.</p> <p>Following initial recognition, property, plant and equipment may be carried at their depreciated cost or their fair value in accordance with the accounting policy adopted by management.</p>	<p>Management performed an analysis of the company's property, plant and equipment and none of the assets is considered to have significant parts with a specific useful life. Also, the Company has reviewed its depreciation methods for its assets and their estimated useful lives.</p> <p>Given the nature of the capital assets, management will use the depreciated cost model. Management does not believe that presentation at fair value has significant benefits, given the difficulties associated with determining fair value and managing fair value in accounting systems.</p>
IFRS 8 Operating Segments	<p>The IFRS requires an entity to report financial and descriptive information about its reportable segments.</p>	<p>Management reviewed the application of this provision and determined that it operates only in one segment—specifically the research & development including enzyme enhanced carbon capture technology.</p>

Controls and Procedures

The Company complies with the requirements of the Canadian Securities Administrator's Multilateral Instrument 52-109.

Additional and Continuous Disclosure

This analysis was prepared on September 29, 2011. Additional disclosure is provided on the SEDAR Web site at: www.sedar.com.

MANAGEMENT'S REPORT

The CO₂ Solution Inc. financial statements and other financial information provided in this annual report are the responsibility of the Company's management and have been reviewed and approved by the Board of Directors. These financial statements were drawn up in accordance with Canadian generally accepted accounting principles and include amounts established in accordance with management's best estimates, based upon a conservative approach. The selection of accounting principles and methods rests with management.

The Company maintains internal accounting and administrative control systems designed to ensure the relevance and reliability of the financial information and the protection of the Company's assets.

Management acknowledges its responsibility in managing the Company's business according to the requirements of the relevant laws and accepted standards and financial principles, in addition to maintaining appropriate standards of conduct in its activities.

The Board of Directors exercises its supervision of the financial statements and other financial information through its audit committee, which is composed exclusively of directors who are not members of CO₂ Solution Inc.'s management team.

This committee's duties consist of examining the financial statements and recommending their approval to the Board

of Directors, examining internal accounting and information security systems and any other aspect of the Company's accounting and finance department. In order to do so, the audit committee conducts regular meetings with the external auditors in the presence or absence of Company management, for the purpose of reviewing their audit plan and discussing the results of their work.

The external auditors are appointed to report to the shareholders regarding the fairness of the presentation of the Company's financial statements. The auditors fulfill this responsibility by carrying out an independent examination of these statements in accordance with Canadian generally accepted auditing standards.

On behalf of Management,

September 29, 2011



Glenn R. Kelly

President and Chief Executive Officer



Thom Skinner, CA

Senior Vice President, Finance and Chief Financial Officer

INDEPENDENT AUDITORS' REPORT

To the Shareholders of CO₂ Solution Inc.

We have audited the accompanying consolidated financial statements of CO₂ Solution Inc., which comprise the consolidated balance sheets as at June 30, 2011 and 2010 and the consolidated statements of earnings and comprehensive income, contributed surplus, deficit and cash flows for the years then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

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

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the

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

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of CO₂ Solution Inc. as at June 30, 2011 and 2010 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

*Raymond Chabot Grant Thornton LLP*¹
Chartered Accountants
Québec, September 29, 2011

¹ Chartered accountant auditor permit no. 13790

CO₂ Solution Inc.

Consolidated Earnings and Comprehensive Income

YEARS ENDED JUNE 30, 2011 AND 2010

	2011	2010
	\$	\$
Revenues	1,914,118	10,118
Cost of revenues	28,701	385
Gross profit	1,885,417	9,733
Costs and operating expenses		
Research and development expenses, net	917,686	269,266
Business development expenses	769,523	532,983
General and administrative expenses	1,472,429	1,297,105
Net interest earned from carrying charges (Note 4)	(6,668)	(19,177)
	3,152,970	2,080,177
Net loss and comprehensive income	(1,267,553)	(2,070,444)
Basic and diluted loss per share (Note 15)	(0.02)	(0.04)

The accompanying notes are an integral part of the consolidated financial statements and Note 3 provides other information on earnings.

CO₂ Solution Inc.

Consolidated Contributed Surplus

Consolidated Deficit

YEARS ENDED JUNE 30, 2011 AND 2010

	2011	2010
	\$	\$
CONSOLIDATED CONTRIBUTED SURPLUS		
Balance, beginning of year	2,714,374	2,110,244
Stock options expired (Note 13)	3,661	15,413
Stock options cancelled (Note 13)	260	3,516
Warrants cancelled (Note 12)		585,201
Balance, end of year	2,718,295	2,714,374
CONSOLIDATED DEFICIT		
Balance, beginning of year	15,979,708	13,822,771
Net loss	1,267,553	2,070,444
Share issue expenses (Note 12)		86,493
Balance, end of year	17,247,261	15,979,708

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

CO₂ Solution Inc.**Consolidated Cash Flows****YEARS ENDED JUNE 30, 2011 AND 2010**

	2011	2010
	\$	\$
OPERATING ACTIVITIES		
Net loss	(1,267,553)	(2,070,444)
Items not affecting cash and cash equivalents		
Amortization	87,123	86,590
Consultant fees in consideration for warrants	41,232	37,796
Stock-based compensation	155,623	86,569
	<u>(983,575)</u>	<u>(1,859,489)</u>
Change in non-cash working capital items		
Accounts receivable, excluding government assistance	(630,639)	(14,990)
Government assistance receivable	51,457	(39,701)
Tax credits receivable	(510,931)	(6,602)
Prepaid expenses	(30,331)	3,608
Accounts payable and accrued liabilities	115,873	137,920
	<u>(1,004,571)</u>	<u>80,235</u>
Cash flows from operating activities	<u>(1,988,146)</u>	<u>(1,779,254)</u>
INVESTING ACTIVITIES		
Temporary investments	1,822,397	(465,331)
Amounts capitalized to patents	(142,080)	(87,484)
Additions to property, plant and equipment	(42,143)	(14,236)
Cash flows from investing activities	<u>1,638,174</u>	<u>(567,051)</u>
FINANCING ACTIVITIES		
Note payable to a shareholder		475,000
Refundable contribution	99,055	
Deferred credits	6,850	1,462
Share issues	5,000	2,000,000
Share issue expenses		(86,493)
Cash flow from financing activities	<u>110,905</u>	<u>2,389,969</u>
Net increase (decrease) in cash	(239,067)	43,664
Cash, beginning of year	<u>372,180</u>	<u>328,516</u>
Cash, end of year	<u>133,113</u>	<u>372,180</u>


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

CO₂ Solution Inc.
Consolidated Balance Sheets
JUNE 30, 2011 AND 2010

	2011	2010
	\$	\$
ASSETS		
Current assets		
Cash	133,113	372,180
Temporary investments (Note 5)	187,628	2,010,025
Accounts receivable (Note 6)	665,515	86,333
Tax credits receivable	1,220,797	709,866
Prepaid expenses	52,685	22,354
	2,259,738	3,200,758
Property, plant and equipment (Note 7)	234,289	247,113
Patents (Note 8)	418,410	317,942
	2,912,437	3,765,813
LIABILITIES		
Current liabilities		
Accounts payable and accrued liabilities	459,573	343,700
Note payable to a shareholder having a significant influence, without interest, maturing in February 2011		475,000
	459,573	818,700
Refundable contribution (Note 10)	99,055	
Deferred credits (Note 11)	35,367	37,973
Note payable to a shareholder having a significant influence, without interest or repayment terms	475,000	
	1,068,995	856,673
SHAREHOLDERS' EQUITY		
Capital stock (Notes 12 and 21)	15,684,667	15,675,834
Stock options (Note 13)	608,713	460,844
Warrants (Notes 12 and 21)	79,028	37,796
Contributed surplus	2,718,295	2,714,374
Deficit	(17,247,261)	(15,979,708)
	1,843,442	2,909,140
	2,912,437	3,765,813
Commitments (Note 18)		
Contingencies (Note 19)		

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

On behalf of the Board,



 Evan Price
 Director



 Glenn Kelly
 Director

CO₂ Solution Inc.

Notes to Consolidated Financial Statements

JUNE 30, 2011 AND 2010

1 - GOVERNING STATUTE AND NATURE OF OPERATIONS

CO₂ Solution Inc. ("CO₂ Solution" or the "Company"), incorporated under the Business Corporations Act (Quebec), is a high technology enterprise involved in the capture and management of carbon dioxide (CO₂). More specifically, the Company is currently focused on commercializing an enzyme-based enabling technology for efficient CO₂ capture from fossil fuel power plants and other large emitters of CO₂. The Company intends to continue its research and development and commercialization efforts. The Company's operations are subject to all the inherent risks related to running an emerging high technology company, such as successfully completing its research and development activities, negotiating collaborative working agreements and commercialization of its enzyme technology and obtaining the required financing.

2 - SIGNIFICANT ACCOUNTING POLICIES

Consolidated financial statements

The consolidated financial statements include the accounts of CO₂ Solution Inc. and those of CO₂ Solution Technologies Inc., 9157-4400 Québec Inc., 9157-4426 Québec Inc., 9157-4475 Québec Inc., and Fiducie Financière CO₂ Solution.

Accounting estimates

The preparation of financial statements in accordance with Canadian generally accepted accounting principles requires management to make estimates that affect the amounts of assets and liabilities reported in the financial statements. Those estimates also affect the disclosure of contingencies at the date of the financial statements and the reported amounts of revenues and expenses during the year. Significant estimates include, but are not limited to, tax credits receivable, the useful lives and recoverable value of property, plant and equipment and intangible assets and certain accrued liabilities. Actual results could differ from those estimates.

Basis of presentation

The financial statements are prepared using the historical cost method, except for certain financial instruments that are recognized at fair value. No information on fair value is presented when the carrying amount corresponds to a reasonable approximation of the fair value.

Financial assets and liabilities

On initial recognition, all financial assets and liabilities are measured and recognized at their fair value, except for financial assets and liabilities resulting from certain related party transactions.

Financial assets are classified as held for trading, held to maturity, available for sale, or loans and receivables. Financial liabilities are classified as held for trading or other liabilities. Financial instruments held for trading are measured at fair value, with gains and losses recognized in net income. Under the standard, entities may classify any financial instrument as held for trading on initial recognition or on adoption of the standard, even if the financial instrument did not meet the definition of a financial instrument held for trading.

CO₂ Solution Inc.

Notes to Consolidated Financial Statements

JUNE 30, 2011 AND 2010

2 - SIGNIFICANT ACCOUNTING POLICIES (Continued)

The financial instruments classified as loans, receivables and other liabilities are measured at amortized cost.

The fair value of a financial instrument is the amount at which the financial instrument could be exchanged in an arm's length transaction between knowledgeable and willing non-related parties. Fair value is based on active market prices. If active market prices are not available, fair value is based on prevailing market prices for instruments with similar characteristics and risk profiles using observable market-based inputs.

Cash is classified as held for trading, while accounts receivable, except for indirect taxes and government assistance receivable, are classified as loans and receivables. Accounts payable and accrued liabilities, note payable and refundable contribution are classified as other financial liabilities.

Term deposits are designated as held for trading because the Company believes that the financial information generated by this classification is more relevant for decision-making and provides better means for evaluating the Company's performance.

For the fair value hierarchy according to Section 3862 of the *Canadian Institute of Chartered Accountants' Handbook*, the fair value of cash and term deposits is established at Level 1. The fair value is determined directly by reference to unadjusted quoted prices in active markets for identical assets and liabilities.

Cash and cash equivalents

The Company's policy is to present cash and temporary investments having a term of three months or less from the acquisition date with cash and cash equivalents.

Amortization

Property, plant and equipment are recorded at cost and amortized over their estimated useful lives using the following methods, annual rates and period:

	<u>Methods</u>	<u>Rates and period</u>
Laboratory equipment, layout and office equipment	Diminishing balance	20%
Computer equipment	Diminishing balance	30%
Leasehold improvements	Straight-line	10 years

Patents, obtained or pending, are recorded at cost and amortized on a straight-line basis over 20 years.

Impairment of long-lived assets

Property, plant and equipment and patents are tested for recoverability when events or changes in circumstances indicate that their carrying amount may not be recoverable. The carrying amount of a long-lived asset is not recoverable when it exceeds the sum of the undiscounted cash flows expected from its use and eventual disposal. In such a case, an impairment loss must be recognized and is equivalent to the excess of the carrying amount of a long-lived asset over its fair value.

CO₂ Solution Inc.

Notes to Consolidated Financial Statements

JUNE 30, 2011 AND 2010

2 - SIGNIFICANT ACCOUNTING POLICIES (Continued)

Research and development expenses

Expenses related to research and development activities are expensed as incurred, except for development expenses which meet capitalization criteria according to Canadian generally accepted accounting standards, in which case they are deferred and amortized.

Share issue expenses

Share issue expenses are recognized directly in the consolidated statement of deficit.

Tax credits and government assistance

Tax credits and government assistance are accounted for in the year during which the related expenses are incurred, provided the Company has reasonable assurance that these amounts will be recovered. Tax credits and government assistance related to property, plant and equipment are recorded as deferred credits in the balance sheet and are amortized using the same rates as those used for the related assets. Those relating to amounts expensed in earnings are applied against the related costs. The tax credits must be reviewed and approved by the tax authorities, accordingly, the amounts granted may differ from the amounts recorded (Note 19).

Income taxes

The Company uses the liability method of accounting for income taxes. Under this method, future income tax assets and liabilities are determined according to deductible or taxable temporary differences between the carrying amounts and tax bases of assets and liabilities. They are measured by applying enacted or substantively enacted tax rates and laws at the date of the financial statements for the years in which the temporary differences are expected to reverse.

The Company establishes a valuation allowance against future income tax assets if, based on available information, it is more likely than not that some or all the future income tax assets will not be realized.

Foreign currency translation

Monetary assets and liabilities in foreign currency are translated into Canadian dollars at the exchange rate in effect at the balance sheet date. Revenues and expenses are translated at the exchange rate at the time of the transaction.

Employee future benefits

The Company has set up a simplified defined contribution pension plan. The Company's contribution is limited to the amount provided under the plan, which is equal to the employee's contribution up to 2% of gross earnings. Pension expense is recognized in earnings for the year during which the amounts are due.

CO₂ Solution Inc.

Notes to Consolidated Financial Statements

JUNE 30, 2011 AND 2010

2 - SIGNIFICANT ACCOUNTING POLICIES (Continued)

Revenue recognition

The Company's revenue is derived from research contracts, design, development and marketing of goods and services related to the management and elimination of CO₂.

The Company recognizes revenue from research contracts when the research activities under the contract are carried out, the contract amount is fixed and collection is reasonably assured.

These contracts usually provide for one-time payments (upfront payments) and payments for research services in the form of cost reimbursements and milestone payments.

The Company entered into certain research and development agreements comprising several components. Such arrangements are divided into separate units of accounting provided that the delivered item has stand-alone value and there is objective and reliable evidence of the fair value of the undelivered items. When the arrangements cannot be divided into separate units of accounting, the arrangements are considered arrangements with a single deliverable.

If reliable and objective evidence of fair value for each deliverable is available, the total arrangement consideration is allocated to the units of accounting based on their relative fair value. However, if evidence of fair value is only available for undelivered items, the arrangement consideration is allocated first to the undelivered items based on their fair value, with the remainder being allocated to the delivered items, using the residual method.

Revenue for each unit of accounting or arrangement with a single deliverable is recognized according to the Company's revenue recognition policies as previously disclosed. When recognition criteria are not respected, deferred revenue is recognized for the amounts received.

Investment income is recognized using the accrual method. Interest income is recognized according to the number of days the investment is held during the year.

Earnings per share

Basic earnings per common share are calculated by dividing net earnings available for common shareholders by the weighted average number of common shares outstanding during the year. Diluted earnings per share are calculated taking into account the potential dilution that would result if the common share stock options and warrants were exercised or converted into common shares at the later of the beginning of the period or their issue date. The dilution effect is determined using the treasury stock method for the stock options and the warrants.

Stock-based compensation

The Company maintains a stock-based compensation plan which is described in Note 13. The Company recognizes a compensation expense in the financial statements for all types of stock-based compensation granted to directors, executives and employees of the Company and consultants, including stock options, using the fair-value based method established according to the Black-Scholes model. Compensation expense is recognized over the applicable vesting period with a corresponding increase in shareholders' equity under Stock options. When stock options are exercised, the exercise price and the related portion previously recorded in Stock options are credited to capital stock.

CO₂ Solution Inc.

Notes to Consolidated Financial Statements

JUNE 30, 2011 AND 2010

3 - INFORMATION INCLUDED IN CONSOLIDATED EARNINGS

	2011	2010
	\$	\$
Research and development expenses	1,693,926	775,883
Tax credits related to research and development expenses	(504,078)	(430,813)
Government assistance	(272,162)	(75,804)
Amortization of property, plant and equipment	54,967	62,785
Amortization of patents	41,612	33,576
Amortization of deferred credits	(9,456)	(9,771)
Employee future benefits	14,028	11,216

4 - NET INTEREST EARNED FROM CARRYING CHARGES

	2011	2010
	\$	\$
Other financial expenses	6,940	4,347
Interest income	(13,608)	(23,524)
	(6,668)	(19,177)

5 - TEMPORARY INVESTMENTS

	2011	2010
	\$	\$
Term deposits, 0.12% and 0.50% (0.50% and 0.56% as at June 30, 2010), maturing in June 2012 and August 2011	187,628	2,010,025

6 - ACCOUNTS RECEIVABLE

	2011	2010
	\$	\$
Trade accounts	619,625	51,457
Government assistance		31,820
Indirect taxes	45,800	3,056
Other	90	86,333
	665,515	86,333

7 - PROPERTY, PLANT AND EQUIPMENT

	2011		
	Cost	Accumulated amortization	Net
	\$	\$	\$
Laboratory equipment and layout	735,979	576,041	159,938
Computer equipment	66,670	34,277	32,393
Office equipment	131,458	102,511	28,947
Leasehold improvements	31,674	18,663	13,011
	965,781	731,492	234,289

CO₂ Solution Inc.

Notes to Consolidated Financial Statements

JUNE 30, 2011 AND 2010

7 - PROPERTY, PLANT AND EQUIPMENT (Continued)

	2010		
	Cost	Accumulated amortization	Net
	\$	\$	\$
Laboratory equipment and layout	711,016	540,864	170,152
Computer equipment	49,490	24,891	24,599
Office equipment	131,458	95,274	36,184
Leasehold improvements	31,674	15,496	16,178
	923,638	676,525	247,113

8 - PATENTS

	2011		
	Cost	Accumulated amortization	Net
	\$	\$	\$
Patents	718,668	300,258	418,410

	2010		
	Cost	Accumulated amortization	Net
	\$	\$	\$
Patents	576,588	258,646	317,942

9 - BANK LOAN

As of June 30, 2011, the Company has an available unused authorized line of credit of \$100,000, bearing interest at the prime rate plus 2.25% (5.25%; 5.5% as at June 30, 2010), secured by a term deposit of \$60,000 and renegotiable in October 2011.

Under this line of credit, the Company must maintain a minimum working capital ratio of 1.5:1 and a total debt/equity ratio not exceeding 3:1. As of June 30, 2011, the Company is in compliance with these ratios.

10 - REFUNDABLE CONTRIBUTION

The Company obtained from Economic Development of Canada a refundable contribution of up to \$250,000 of which \$111,820 was received during the year. This contribution is refundable starting January 2014 with equal annual payments representing 4% of the Company's total income. The loan was accrued to a present value of \$97,820, using an estimated capitalization rate of 5%. The difference between the present value and the principal amount of the loan is included with revenues shown in the statement of earnings.

CO₂ Solution Inc.

Notes to Consolidated Financial Statements

JUNE 30, 2011 AND 2010

11 - DEFERRED CREDITS

	2011	2010
	\$	\$
Government assistance and tax credits on laboratory equipment and layout		
Government assistance	4,410	5,513
Tax credits	30,957	32,460
	35,367	37,973

12 - CAPITAL STOCK

Authorized

Unlimited number of common shares, without par value, voting and participating

Issued and fully paid

The following table shows the changes in the Company's capital stock during the years ended June 30, 2011 and 2010:

	2011		2010	
	Number	\$	Number	\$
Balance, beginning of year	60,261,136	15,675,834	50,261,136	13,675,834
Issue following private investments*			10,000,000	2,000,000
Exercise of options	25,000	8,833		
Balance, end of year	60,286,136	15,684,667	60,261,136	15,675,834

* In December 2009, pursuant to a private investment, the Company issued 10,000,000 shares for a gross revenue of \$2,000,000. In connection with this transaction, issue expenses of \$86,493 were paid and recognized in the consolidated statement of deficit.

The following table shows the changes in the Company's warrants during the years ended June 30, 2011 and 2010:

	2011		2010	
	Number	Weighted average exercise price	Number	Weighted average exercise price
		\$		\$
Outstanding, beginning of year	1,000,000	0.24	16,581,428	0.28
Granted			1,000,000	0.24
Cancelled			(16,581,428)	0.28
Outstanding, end of year	1,000,000	0.24	1,000,000	0.24

CO₂ Solution Inc.

Notes to Consolidated Financial Statements

JUNE 30, 2011 AND 2010

12 - CAPITAL STOCK (Continued)

The outstanding warrants as at June 30, 2011 are those issued in connection with an agreement concluded in December 2009 with a consultant. They have a fair value of \$123,700, give the right to acquire one common share for \$0.24 and expire in August 2013. Related expense is amortized over 36 months as research and development expenses in the consolidated statements of earnings.

13 - STOCK OPTIONS

The Company has a stock option plan for directors, executives, employees and consultants. All the options granted under the terms of the plan may be exercised within a maximum five-year period commencing on the date of grant. The Board of Directors designates the optionees and determines the number of common shares involved in each of these options, the vesting date, the exercise price, the expiry date, the terms of acquisition and any restrictions on the exercise of the options. The share acquisition price must not be less than the closing price on the day prior to the date of grant of these shares.

The maximum number of common shares issued under the terms of the plan was established at 6,026,114, which corresponds to 10% of the issued and outstanding shares of capital stock on the date of the most recent ratification by shareholders. The maximum number that may be granted to a director, executive or employee of the Company or to a consultant cannot exceed 5% of all the outstanding common shares.

The following table summarizes information about outstanding and exercisable stock options for the years ended June 30, 2011 and 2010:

	2011		2010	
	Number	Weighted average exercise price	Number	Weighted average exercise price
		\$		\$
Outstanding, beginning of year	3,955,440	0.22	3,168,140	0.24
Granted	920,000	0.19	857,600	0.18
Expired	(17,900)	0.35	(30,300)	0.82
Cancelled	(1,700)	0.20	(40,000)	0.24
Exercised	(25,000)	0.20		
Outstanding, end of year	4,830,840	0.22	3,955,440	0.22

CO₂ Solution Inc.

Notes to Consolidated Financial Statements

JUNE 30, 2011 AND 2010

13 - STOCK OPTIONS (Continued)

As at June 30, 2011, the following outstanding stock options had been granted:

Outstanding options			Exercisable options	
Number	Weighted average exercise price	Weighted average remaining contractual life (years)	Number	Weighted average exercise price
	\$			\$
347,600	0.16	3.30	322,600	0.16
350,000	0.18	3.70	116,666	0.18
539,800	0.52	0.90	539,800	0.52
10,000	0.30	2.20	10,000	0.30
150,000	0.20	3.80	150,000	0.20
10,000	0.19	2.30	10,000	0.19
1,769,140	0.18	2.20	1,769,140	0.18
761,000	0.17	1.80	608,800	0.17
418,300	0.20	4.40	240,000	0.20
450,000	0.17	4.70	112,500	0.17
25,000	0.31	4.90		
<u>4,830,840</u>	<u>0.22</u>	<u>2.70</u>	<u>3,879,506</u>	<u>0.23</u>

Options issued prior to November 2009 vest as follow: 20% upon signature and the remaining 80% is gradually acquired at the rate of 20% per year, over 4 years, except for the President whose vesting period is 100% upon signature, as well as for consultants for which the expenses are recognized when services are rendered.

Options issued after November 2009 vest gradually at the rate of 25,000 options every 6 months, up to a maximum period of 3 years, except for the President and CEO and the Senior Vice-President Finance and Chief Financial Officer whose vesting period is respectively 58,333 and 112,500 options every 6 months from the date of the grant up to a maximum period of 3 years.

CO₂ Solution Inc.

Notes to Consolidated Financial Statements

JUNE 30, 2011 AND 2010

13 - STOCK OPTIONS (Continued)

The fair value of the options are determined according to the Black-Scholes option pricing model based on the following weighted average assumptions:

	<u>2011</u>	<u>2010</u>
	Employees, directors and executives	Employees, directors and executives
Risk-free interest rate	2.31%	1.91%
Expected volatility	103.76%	99.67%
Annual dividend yield	Nil	Nil
Expected life of each option granted	5 years	5 years
Fair value of each option granted	\$0.14	\$0.12

For the year ended June 30, 2011, the Company recorded a \$155,623 compensation expense (\$86,569 in 2010) for awards of stock-based compensation to employees, of which \$43,088 are recorded in development business expenses (\$19,903 in 2010) and \$112,535 in general and administrative expenses (\$66,666 in 2010).

The following table presents changes in stock options for the years ended June 30, 2011 and 2010:

	<u>2011</u>	<u>2010</u>
	\$	\$
Balance, beginning of year	460,844	393,204
Stock-based compensation	155,623	86,569
Stock options exercised	(3,833)	
Stock options cancelled	(260)	(18,929)
Stock options expired	(3,661)	
Balance, end of year	608,713	460,844

CO₂ Solution Inc.

Notes to Consolidated Financial Statements

JUNE 30, 2011 AND 2010

14 - INCOME TAXES

The reconciliation between income tax recovery at statutory rates and the income tax provision is detailed as follows:

	2011		2010	
	\$	%	\$	%
Income tax saving at statutory rates	378,998	29.90	629,415	30.40
Related differences in tax rates of CO ₂ Solution Technologies Inc.	(18,203)	(1.44)	(116,600)	(5.63)
Provincial income tax credits non-taxable in Quebec	39,426	3.11	18,571	0.89
Non-deductible stock-based compensation	(46,531)	(3.67)	(26,750)	(1.29)
Change in income tax rates	(6,338)	(0.50)	(87,593)	(4.23)
Expired tax losses			(156,438)	(7.55)
Other	(28,108)	(2.22)	44,426	2.14
Valuation allowance	(319,244)	(25.19)	(305,031)	(14.73)
Income tax provision				

Future income tax assets and liabilities arise from variances between the carrying amounts and tax bases of the following amounts:

	2011	2010
	\$	\$
Future income tax assets (liabilities) resulting from the following:		
Property, plant and equipment	162,943	156,014
Development expenses	(62,647)	(51,499)
Share issue expenses	21,471	41,797
Research and development expenses	913,866	945,399
Tax losses	2,164,992	1,789,670
Net future income tax assets	3,200,625	2,881,381
Valuation allowance	(3,200,625)	(2,881,381)
Net future income tax assets recorded		

As of June 30, 2011, for federal and provincial income tax purposes, the Company has accumulated non-capital losses of approximately \$9,013,000 and \$8,292,000, respectively. These losses can be carried forward against future years' taxable income and expire no later than 2031.

CO₂ Solution Inc.

Notes to Consolidated Financial Statements

JUNE 30, 2011 AND 2010

14 - INCOME TAXES (Continued)

As of June 30, 2011, non-capital losses are detailed as follows:

	Federal	Provincial
	\$	\$
2014	115,000	87,000
2015	1,235,000	1,141,000
2026	1,026,000	638,000
2027	742,000	752,000
2028	1,066,000	1,059,000
2029	1,501,000	1,298,000
2030	1,924,000	1,913,000
2031	1,404,000	1,404,000
	<u>9,013,000</u>	<u>8,292,000</u>

Some research and development expenses incurred by the Company can be carried forward against future years' taxable income. These unclaimed deductions, which can be carried forward indefinitely, amount to approximately \$2,253,000 for federal purposes and \$6,636,000 for provincial purposes.

As at June 30, 2011, federal investment tax credits which are deductible from tax payable are detailed as follows:

Expiration date	\$
2014	65,400
2015	161,000
2026	2,700
2027	6,000
2028	1,000
2029	11,000
2030	2,200
2031	7,200
	<u>256,500</u>

Loss carryforwards and research and development expenses could be subject to a review and possible adjustment by the tax authorities.

15 - EARNINGS PER SHARE

The following table summarizes the basic and diluted weighted average number of shares outstanding used in the basic and diluted loss per share calculations:

	2011	2010
	\$	\$
Basic and diluted weighted average number of shares outstanding	<u>60,275,720</u>	<u>55,658,396</u>

CO₂ Solution Inc.

Notes to Consolidated Financial Statements

JUNE 30, 2011 AND 2010

15 - EARNINGS PER SHARE (Continued)

For the years ended June 30, 2011 and 2010, the basic weighted average number of shares outstanding was the same as the diluted weighted average number of shares since the effect of stock options and warrants described in Notes 12 and 13 would have been anti-dilutive because the Company has incurred net losses. Accordingly, the diluted loss per share for these years was calculated using the basic weighted average number of shares outstanding.

16 - FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES, FINANCIAL RISKS AND FAIR VALUE OF FINANCIAL INSTRUMENTS

Financial risk management objectives and policies

The Company is exposed to various financial risks resulting from both its operations and its investment activities. Company's management is responsible for financial risk management.

The Company does not enter into contracts concerning financial instruments, including derivatives, for speculative purposes.

Financial risks

The Company's main financial risk exposure and its financial risk management policies are as follows.

Credit risk

The financial instruments that potentially expose the Company to a credit risk consist of cash, temporary investments and accounts receivable. As at June 30, 2011, the Company had \$133,113 in cash on hand, \$187,628 in temporary investments with a recognized financial institution and \$619,125 in trade accounts, which management believes to represent a low risk of loss.

Trade accounts receivable

The Company's credit risk is primarily attributable to its trade accounts receivable. The Company does not require a guarantee from its customers. The Company's policy is to have each customer undergo a credit check. Moreover, trade account receivable balances are managed and analyzed on an ongoing basis and, accordingly, the Company's exposure to doubtful accounts is not significant.

As at June 30, 2011, two customers account for 29% and 61%, respectively, of the accounts receivable.

Exchange risk

The Company is exposed to foreign exchange risk due to accounts receivables denominated in US dollars which total \$619,125 (\$0 in 2010) as at June 30, 2011.

The Company does not enter into arrangements to hedge its foreign exchange risk.

CO₂ Solution Inc.

Notes to Consolidated Financial Statements

JUNE 30, 2011 AND 2010

16 - FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES, FINANCIAL RISKS AND FAIR VALUE OF FINANCIAL INSTRUMENTS (Continued)

Interest rate risk

The Company is exposed to a limited interest rate risk since all its temporary investments bear interest at a fixed rate. The Company is, however, exposed to a fair value risk on its investments resulting from interest rate fluctuations.

The bank loan bears interest at a variable rate and, therefore, the Company is exposed to the cash flow risk resulting from interest rate fluctuations.

Liquidity risk

The Company manages its liquidity needs by following up regularly on cash expenditures as part of its daily activities. The Company establishes budget estimates and cash flow forecasts to ensure that it has the funds required to fulfill its obligations.

The Company's strategy is to keep on hand cash and term deposits to meet its cash needs for a minimum of 30 days. The Company's financial liabilities mature in less than six months, except the note payable to a shareholder and refundable contribution.

Fair value of financial instruments

The fair value of note payable to a shareholder could not be determined because it is practically impossible to find financial instruments on the market having substantially the same economic characteristics.

17 - CAPITAL MANAGEMENT

The Company manages its capital with the aim of maintaining a flexible capital structure that optimizes the cost of capital at an acceptable risk. For purposes of capital management, capital is defined by shareholders' equity minus cash and temporary investments (\$1,522,701 in 2011 and \$526,935 in 2010). The Company monitors its capital by watching its monthly cash consumption and short-term commitments related to its financial liabilities. The Company is under no capital requirements imposed by third parties.

18 - COMMITMENTS

Royalties

Following the sale of the technology agreement dated May 21, 1998, and amended March 3, 2004, the Company reached agreement with a former director having a controlling interest in the Company to pay him a royalty corresponding to 5% of cumulative gross earnings exceeding \$5,000,000, calculated based on the Company's audited annual financial statements. The maximum amount of royalties has been set at \$1,000,000 for the period ending January 1, 2021.

Lease agreements

The Company has entered into a lease agreement expiring in February 2015 which calls for lease payments of \$545,171 for the rental of premises. Minimum payments for the next years are \$153,258 in 2012, \$152,209 in 2013, \$151,392 in 2014 and \$88,312 in 2015.

CO₂ Solution Inc.

Notes to Consolidated Financial Statements

JUNE 30, 2011 AND 2010

19 - CONTINGENCIES

In July 2010, a draft notice of assessment from the Canada Revenue Agency was received by CO₂ Solution Technologies Inc. questioning its status as a Canadian-controlled private corporation (CCPC). CO₂ Solution Technologies Inc. is a consolidated variable interest entity. The draft assessment focused on the fiscal year ended June 30, 2009 and, as a consequence, research and development tax credits claimed by CO₂ Solution Technologies Inc. for that year and included in the Company's balance sheet as at June 30, 2009 and 2010 were refused, and credits to be claimed for the year ended June 30, 2011 could be refused. In the opinion of CO₂ Solution Technologies Inc. and the Company's management, these credits are receivable according to the CCPC status of CO₂ Solution Technologies Inc., but their receipt depends on the successful resolution of this matter. CO₂ Solution Technologies Inc. intends to firmly defend its position since it judges that the draft of notice of assessment is unfounded and that CO₂ Solution Technologies Inc.'s position will ultimately prevail. Under the circumstances, no provision for this item has been made in the accounts of CO₂ Solution Technologies Inc. or in the consolidated statements of the Company.

In July 2011, Revenu Québec notified Fiducie Financière CO₂ Solution of its intention to issue an assessment (hereinafter the "draft assessment") and modify the tax treatment of certain capital transactions between CO₂ Solution Inc. and some of its consolidated variable interest entities, namely CO₂ Solution Technologies Inc. and Fiducie Financière CO₂ Solution, which occurred during the December 31, 2008 taxation year of Fiducie Financière CO₂ Solution. The draft assessment focused on the transfer of \$2 millions between the entities and questioned whether this amount should have been treated as a taxable dividend in the accounts of Fiducie Financière CO₂ Solution. In the opinion of Fiducie Financière CO₂ Solution, the Company's management and their advisors, this transfer of funds between the entities was a movement of capital between the entities and not an income item subject to any taxation, Revenu Québec's claim is unfounded and the proposed tax treatment of the transferred funds as a dividend of \$2 millions in the accounts of Fiducie Financière CO₂ Solution is incorrect. Fiducie Financière CO₂ Solution intends to firmly defend its position and is of the opinion that its tax filing position will ultimately prevail. Under the circumstances, no provision for this item has been made in the accounts of Fiducie Financière CO₂ Solution or in the consolidated statements of the Company.

20 - SEGMENT DISCLOSURE

The Company has examined its activities and determined that it operates in a single reportable segment. This single reportable segment derives its income from the sale of procedures and services relating to the management and elimination of CO₂ using an enzyme conversion-based technology.

The Company earns its income from two clients based in the United States in 2011 and uses its assets in Canada.

CO₂ Solution Inc.

Notes to Consolidated Financial Statements

JUNE 30, 2011 AND 2010

21 - SUBSEQUENT EVENTS

New bank credit line

As at June 30, 2011, the Company benefited from credit facilities in the form of an operating line of credit for an authorized amount of \$100,000, bearing interest at prime plus 2.25% and guaranteed by a \$60,000 term of deposit. As at June 30, 2011, this operating line of credit was unused. Subsequent to the year-end, in July 2011, the Company negotiated a new credit facility with a new bank. This new credit facility is in the form of an operating line of credit of \$150,000 bearing interest at prime rate plus 2% and is secured by a universal charge on the Company's assets to a maximum of \$225,000. The Company must comply with certain financial ratios and the agreement is renewable annually.

Private placement

On August 31, 2011, the Company announced the closing of a brokered private placement of 18,901,700 units at a price of \$0.23 per unit for aggregate gross proceeds of \$4,347,391. Each unit is comprised of one common share of the Company and one-half common share purchase warrant. Each whole warrant entitles the holder to acquire one additional common share of the Company at a price of \$0.28 per common share until August 31, 2013.

Proceeds of the offering will be used by the Company to strengthen its financial base and provide additional working capital for continued development operations and the pursuit of other market opportunities.

All securities issued under this offering have been issued pursuant to exemptions from the prospectus requirements of applicable securities laws and are subject to a 4 month plus one day statutory hold period ending on January 1, 2012. The Company paid its agents an aggregate cash commission of \$304,317 and has issued the agents 1,323,118 non-transferable compensation options to acquire 1,323,118 common shares of the Company, exercisable at a price of \$0.28 per common share until August 31, 2013.

The Company has received an advance ruling from Revenu Québec confirming that the Company is a qualified issuing corporation for the purposes of the Quebec Stock Savings Plan II (QSSP II) and that the common shares forming part of the units are qualified shares for a QSSP II qualified mutual fund.



Management, Board of Directors, and Scientific Advisory Board

Management

Glenn R. Kelly

President and Chief Executive Officer

Thom Skinner, CA

Senior Vice President, Finance and
Chief Financial Officer

Sylvie Fradette, Ph. D., P. Eng.

Chemical Engineering
Vice President
Research and Development

Jonathan A. Carley

Vice President
Business Development

Normand Voyer, Ph. D., Chemist

Vice President
Biocatalysis

Board of Directors

Evan Price^{1,2}

President and Chief Operating Officer
B45 Inc.

Kimberley Okell, Lawyer¹

Vice President, Legal Affairs and
Assistant Corporate Secretary
Vision 7 International ULC

Martin P. Pelletier²

Administrator

Jocelyn Proteau¹

Administrator

Robert Manherz²

Principal
Dundurn Capital Partners Inc.

Glenn R. Kelly

President and Chief Executive Officer
CO₂ Solution Inc.

Alan Shaw, Ph.D.

President and Chief Executive Officer
Codexis, Inc.

Scientific Advisory Board

Romas J. Kazlauskas, Ph. D.

Professor
Biochemistry, Molecular Biology
and Biophysics
University of Minnesota

Geert Versteeg, Ph. D.

Professor and Chairholder
Multiphase Reactions and Process Design
State University, Groningen

Roger Sheldon, Ph. D.

Professor Emeritus
Biocatalysis and Organic Chemistry
Delft University of Technology

Normand Voyer, Ph. D.

Professor and Director
Department of Chemistry
Laval University

¹ Member of the Audit and Corporate Governance Committees

² Member of the Compensation Committee



Shareholder information

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Legal Advisors - Intellectual Property

Leger Robic Richard, S.E.N.C.R.L.
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Montréal, QC H2Z 2B7
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Shareholder's Annual Meeting

Wednesday, November 23, 2011 at 2:30 pm
Pavillon La Laurentienne – Auditorium Jean-Paul Tardif
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Communications and Investor Relations

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CAPTURE

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