

# **BOYUAN CONSTRUCTION GROUP, INC.**



**BOYUAN**

## **ANNUAL REPORT 2018**

- Audited annual consolidated financial statements for the fiscal years ended June 30, 2018
- Management discussion & analysis for the fiscal year ended June 30, 2018

**BOYUAN CONSTRUCTION GROUP, INC.**

**Report and Consolidated Financial Statements  
For the years ended June 30, 2018 and 2017  
(Expressed in US dollars)**

BOYUAN CONSTRUCTION GROUP, INC.

REPORT AND CONSOLIDATED FINANCIAL STATEMENTS  
AS AT AND FOR THE YEARS ENDED JUNE 30, 2018 AND 2017

<u>CONTENTS</u>	<u>PAGE(S)</u>
INDEPENDENT AUDITOR'S REPORT	1 & 2
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION	3 & 4
CONSOLIDATED STATEMENTS OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME	5
CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY	6
CONSOLIDATED STATEMENTS OF CASH FLOWS	7 & 8
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS	9 - 61

## INDEPENDENT AUDITOR'S REPORT

### TO THE SHAREHOLDERS OF BOYUAN CONSTRUCTION GROUP, INC. (incorporated in the Province of Alberta, Canada with limited liability)

We have audited the accompanying consolidated financial statements of Boyuan Construction Group, Inc. and its subsidiaries (collectively referred to as the "Group"), which comprise the consolidated statements of financial position as at June 30, 2018 and 2017, and the consolidated statements of profit or loss and other comprehensive income, consolidated statements of changes in equity and consolidated statements of 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 International Financial Reporting Standards, 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.

#### **Auditors' 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 in our audits is sufficient and appropriate to provide a basis for our audit opinion.

INDEPENDENT AUDITOR'S REPORT

TO THE SHAREHOLDERS OF BOYUAN CONSTRUCTION GROUP, INC. - continued  
(incorporated in the Province of Alberta, Canada with limited liability)

**Opinion**

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Group as at June 30, 2018 and 2017, and its financial performance and cash flows for the years then ended in accordance with International Financial Reporting Standards.

**Deloitte Touche Tohmatsu**  
Certified Public Accountants  
Hong Kong  
September 28, 2018

**BOYUAN CONSTRUCTION GROUP, INC.**

**CONSOLIDATED STATEMENTS OF FINANCIAL POSITION  
AT JUNE 30, 2018 AND 2017**

	<u>NOTES</u>	<u>2018</u> US\$	<u>2017</u> US\$
<b>Non-current assets</b>			
Unbilled revenue	6	28,853,451	32,076,872
Accounts receivable	7(a)	20,413,009	15,488,246
Property and equipment	4	5,546,587	6,380,373
Prepaid lease payments	5	85,763	85,509
Deferred tax assets	16	7,381,754	5,009,091
		<u>62,280,564</u>	<u>59,040,091</u>
<b>Current assets</b>			
Unbilled revenue	6	110,929,636	84,356,234
Accounts receivable	7(a)	49,898,774	48,426,440
Bank notes receivable	7(b)	9,750,832	-
Deposits	8	13,707,647	10,300,761
Advances and prepaid expenses	9	6,735,180	1,758,478
Other receivables		1,555,738	1,146,929
Income taxes recoverable		938,230	-
Inventory		222,706	740,742
Due from related parties	10	811,674	55,139
Prepaid lease payments	5	2,407	5,037
Restricted cash	11(a)	8,546,215	6,825,097
Cash and cash equivalents	11(b)	7,236,990	3,996,016
		<u>210,336,029</u>	<u>157,610,873</u>
<b>Current liabilities</b>			
Borrowings	12	75,299,783	66,776,845
Accounts and other payables and accrued liabilities	13	51,044,466	21,995,357
Bank notes payable	11(a)	24,421,208	10,882,557
Other loans	14	643,698	3,769,693
Convertible debentures	15	5,262,463	1,065,754
Income taxes payable		-	1,897,404
Other financial liabilities	23	350,460	1,736,706
		<u>157,022,078</u>	<u>108,124,316</u>
<b>Net current assets</b>		<u>53,313,951</u>	<u>49,486,557</u>
<b>Non-current liabilities</b>			
Convertible debentures	15	-	4,137,058
Other loan	14	-	8,420
		<u>-</u>	<u>4,145,478</u>
<b>Net assets</b>		<u><u>115,594,515</u></u>	<u><u>104,381,170</u></u>

BOYUAN CONSTRUCTION GROUP, INC.

	<u>NOTES</u>	<u>2018</u> <u>US\$</u>	<u>2017</u> <u>US\$</u>
<b>Equity</b>			
Share capital	18	7,159,175	7,159,175
Reserves	19	<u>108,435,340</u>	<u>97,221,995</u>
		<u>115,594,515</u>	<u>104,381,170</u>

---

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

The consolidated financial statements on pages 3 to 61 were approved and authorized for issue by the Board of Directors on September 28, 2018 and are signed on its behalf by:

“Cailiang Shou”

“Jack Duffy”

---

DIRECTOR

---

DIRECTOR

BOYUAN CONSTRUCTION GROUP, INC.CONSOLIDATED STATEMENTS OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME  
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017

	<u>NOTES</u>	<u>2018</u> US\$	<u>2017</u> US\$
Construction revenue		325,926,266	199,514,045
Costs of construction		<u>(301,525,477)</u>	<u>(182,490,218)</u>
Gross profit		24,400,789	17,023,827
Other income	24	4,790,323	5,994,334
Foreign exchange losses, net		(53,707)	(1,893)
General and administrative expenses	17	(6,116,207)	(6,500,367)
Impairment losses (recognized) reversed on unbilled revenue, net	6	(1,788,067)	1,126,010
Impairment losses recognized on accounts receivable, net	7(a)	(4,972,560)	(3,029,109)
Impairment losses reversed (recognized) on deposits	8	691,525	(587,251)
Interest expense	25	(6,797,110)	(6,050,908)
Gain (loss) on fair value changes of financial guarantee contracts	23	<u>1,386,246</u>	<u>(496,635)</u>
Profit before income taxes		11,541,232	7,478,008
Income taxes	16	<u>(2,820,432)</u>	<u>(2,849,986)</u>
Profit for the year		<u>8,720,800</u>	<u>4,628,022</u>
Other comprehensive income (expense)			
<i>Items that may be subsequently reclassified to profit or loss:</i>			
Exchange difference on translation of foreign operations		<u>2,492,545</u>	<u>(2,503,517)</u>
Total comprehensive income for the year		<u>11,213,345</u>	<u>2,124,505</u>
Earnings per share:	20		
Basic		0.34	0.18
Diluted		<u>0.30</u>	<u>0.17</u>
Weighted average number of common shares outstanding:	20		
Basic		25,423,065	25,421,536
Diluted		<u>32,923,432</u>	<u>34,421,435</u>

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



**BOYUAN CONSTRUCTION GROUP, INC.****CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY  
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

	Share capital US\$	Contributed surplus US\$ (note 19)	Statutory reserve US\$ (note 19)	Convertible debentures equity reserve US\$	Foreign currency translation reserve US\$	Retained earnings US\$	Total equity US\$
Balance at June 30, 2016	<u>7,156,864</u>	<u>7,066,035</u>	<u>11,510,851</u>	<u>4,603,470</u>	<u>1,305,197</u>	<u>70,612,858</u>	<u>102,255,275</u>
Profit for the year	-	-	-	-	-	4,628,022	4,628,022
Exchange difference on translation of foreign operations	-	-	-	-	(2,503,517)	-	(2,503,517)
Total comprehensive income for the year	-	-	-	-	(2,503,517)	4,628,022	2,124,505
Conversion of convertible debentures (note 18)	2,311	-	-	(921)	-	-	1,390
Transfer to reserve	-	-	812,806	-	-	(812,806)	-
Balance at June 30, 2017	<u>7,159,175</u>	<u>7,066,035</u>	<u>12,323,657</u>	<u>4,602,549</u>	<u>(1,198,320)</u>	<u>74,428,074</u>	<u>104,381,170</u>
Profit for the year	-	-	-	-	-	8,720,800	8,720,800
Exchange difference on translation of foreign operations	-	-	-	-	2,492,545	-	2,492,545
Total comprehensive income for the year	-	-	-	-	2,492,545	8,720,800	11,213,345
Transfer to reserve	-	-	2,113,730	-	-	(2,113,730)	-
Balance at June 30, 2018	<u>7,159,175</u>	<u>7,066,035</u>	<u>14,437,387</u>	<u>4,602,549</u>	<u>1,294,225</u>	<u>81,035,144</u>	<u>115,594,515</u>

**BOYUAN CONSTRUCTION GROUP, INC.****CONSOLIDATED STATEMENTS OF CASH FLOWS  
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

	<u>2018</u> US\$	<u>2017</u> US\$
<b>Cash flows (used in) from operating activities</b>		
Profit before income taxes	11,541,232	7,478,008
Items not affecting cash:		
Depreciation and amortization	1,574,448	2,137,877
Impairment losses recognized (reversed) on unbilled revenue, net	1,788,067	(1,126,010)
Impairment losses recognized on accounts receivable, net	4,972,560	3,029,109
Impairment losses (reversed) recognized on deposits	(691,525)	587,251
Interest expense	6,797,110	6,050,908
(Gain) loss on fair value changes of financial guarantee contracts	(1,386,246)	496,635
Loss on disposal of property and equipment	889	55,284
Unrealized foreign exchange losses, net	(632,696)	(300,034)
Changes in non-cash working capital items:		
Unbilled revenue	(22,387,030)	55,550,060
Accounts receivable	(9,859,514)	(34,030,542)
Bank notes receivable	(10,885,925)	-
Deposits	(3,050,944)	(4,107,034)
Advances and prepaid expenses	(4,926,046)	(1,161,458)
Other receivables	(388,489)	179,061
Inventory	535,538	65,213
Accounts and other payables and accrued liabilities	29,533,257	(14,116,706)
Cash (used in) from operations	2,534,686	20,787,622
Income taxes paid	(8,053,831)	(3,864,320)
	<u>(5,519,145)</u>	<u>16,923,302</u>
<b>Cash flows (used in) from investing activities</b>		
Withdrawal of restricted cash	10,397,923	30,554,217
Placement of restricted cash	(11,984,896)	(23,254,837)
Proceeds from disposal of property and equipment	2,725	57,409
Purchase of property and equipment	(571,817)	(693,433)
Advances to related parties	(755,233)	-
	<u>(2,911,298)</u>	<u>6,663,356</u>
<b>Cash flows from (used in) financing activities</b>		
Repayment of borrowings	(71,079,549)	(91,785,830)
Repayment of bank notes payable	(14,348,375)	(27,351,207)
Repayment of other loans	(3,924,196)	(5,746,642)
Interests paid on bank loans and bank notes payables	(3,988,614)	(4,338,591)
Redemption of convertible debenture	(1,139,125)	(1,155,446)
Interest paid on convertible debentures	(367,184)	(780,606)
Proceeds from borrowings	77,982,053	90,295,681
Proceeds from bank notes payable	27,860,773	19,401,299
Proceeds from other loans	633,465	267,199
	<u>11,629,248</u>	<u>(21,194,143)</u>

BOYUAN CONSTRUCTION GROUP, INC.

	<u>2018</u> US\$	<u>2017</u> US\$
Effect of changes in exchange rate changes on cash and cash equivalents	<u>42,169</u>	<u>(20,746)</u>
Increase in cash and cash equivalents	3,240,974	2,371,769
Cash and cash equivalents, beginning of year	<u>3,996,016</u>	<u>1,624,247</u>
Cash and cash equivalents, end of year, represented by bank balances and cash	<u><u>7,236,990</u></u>	<u><u>3,996,016</u></u>

---

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

1. NATURE OF OPERATIONS

Boyuan Construction Group, Inc. (the "Company") was incorporated under the Canada Business Corporations Act on May 4, 2007, with its shares listed on the Toronto Stock Exchange on June 16, 2010. The Company's registered office and principal place of business is at Jing Hui Plaza, No. 500 Matang Road, Changshui Street, Economic Development Zone, Jiaxing City, Zhejiang Province, People's Republic of China ("China" or "PRC"). The Company and its subsidiaries (collectively the "Group") are engaged in the construction of residential and commercial buildings, municipal infrastructure and engineering projects in the PRC.

2. SIGNIFICANT ACCOUNTING POLICIES

Statement of compliance

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRSs").

The consolidated financial statements were authorized for issue by the Board of Directors of the Company on September 28, 2018.

Basis of preparation

The consolidated financial statements have been prepared on the historical cost basis except for the financial guarantee contracts which are measured at fair value at the end of each reporting period, as explained in the accounting policies set out below.

Historical cost is generally based on the fair value of the consideration given in exchange for goods and services.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, regardless of whether that price is directly observable or estimated using another valuation technique. In estimating the fair value of an asset or a liability, the Group takes into account the characteristics of the asset or liability if market participants would take those characteristics into account when pricing the asset or liability at the measurement date. Fair value for measurement and/or disclosure purposes in these consolidated financial statements is determined on such a basis, except for share-based payment transactions that are within the scope of IFRS 2 *Share-based Payment*, leasing transactions that are within the scope of International Accounting Standards ("IAS") 17 *Leases*, and measurements that have some similarities to fair value but are not fair value, such as net realizable value in IAS 2 *Inventories* or value in use in IAS 36 *Impairment of Assets*.

A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

2. SIGNIFICANT ACCOUNTING POLICIES - continued

Basis of preparation - continued

In addition, for financial reporting purposes, fair value measurements are categorized into Level 1, 2 or 3 based on the degree to which the inputs to the fair value measurements are observable and the significance of the inputs to the fair value measurement in its entirety, which are described as follows:

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the entity can access at the measurement date;
- Level 2 inputs are inputs, other than quoted prices included within Level 1, that are observable for the asset or liability, either directly or indirectly; and
- Level 3 inputs are unobservable inputs for the asset or liability.

The principal accounting policies are set out below.

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and entities (including a special purpose entity) controlled by the Company and its subsidiaries.

Control is achieved when the Company:

- has power over the investee;
- is exposed, or has rights, to variable returns from its involvement with the investee; and
- has the ability to use its power to affect its returns.

The Group reassesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control listed above.

Consolidation of a subsidiary begins when the Group obtains control over the subsidiary and ceases when the Group loses control of the subsidiary. Specifically, income and expenses of a subsidiary acquired or disposed of during the year are included in the consolidated statements of profit or loss and other comprehensive income from the date the Group gains control until the date when the Group ceases to control the subsidiary.

When necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with the Group's accounting policies.

All intragroup assets and liabilities, equity, income, expenses and cash flows relating to transactions between members of the Group are eliminated in full on consolidation.

Cash and cash equivalents

Cash and cash equivalents consist of cash on hand, deposits in banks with an original maturity of 90 days or less.

2. SIGNIFICANT ACCOUNTING POLICIES - continued

Inventory

Inventories are stated at the lower of cost and net realizable value. Costs of inventories are determined on a first-in, first-out method. Net realizable value represents the estimated selling price for inventories less all estimated costs of completion and costs necessary to make the sale.

Property and equipment

Property and equipment including buildings held for use in the production or supply of goods or services, or for administrative purposes (other than construction in progress), are stated in the consolidated statements of financial position at cost less subsequent accumulated depreciation and subsequent accumulated impairment losses, if any.

Depreciation is recognized so as to write off the cost of assets (other than construction in progress) less their residual values over their estimated useful lives, using the straight-line method as follow:

Buildings	30 years, or over the life of the lease, if shorter
Machinery and equipment	10 years
Scaffoldings	5 years
Office equipment	10 years
Vehicles	4 to 5 years
Leasehold improvements	3 years

The estimated useful lives, residual values and depreciation method are reviewed at the end of each reporting period, with the effect of any changes in estimate accounted for on a prospective basis.

Properties in the course of construction for production, supply or administrative purposes are carried at cost, less any recognized impairment loss. Cost includes purchase price of raw materials, consumables used, direct labour and other costs directly attributable to constructing the assets and, for qualifying assets, borrowing costs capitalized in accordance with the Group's accounting policy. Such properties are classified to the appropriate categories of property and equipment when completed and ready for intended use. Depreciation of these assets, on the same basis as other property assets, commences when the assets are ready for their intended use.

An item of property and equipment is derecognized upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on the disposal or retirement of an item of property and equipment is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognized in profit or loss.

2. SIGNIFICANT ACCOUNTING POLICIES - continued

Prepaid lease payments

Prepaid lease payments represent the cost of land use rights paid to the local land bureau of the PRC Government.

Prepaid lease payments are stated in the consolidated statements of financial position at cost, and amortized on a straight-line basis over the period for which the relevant land use rights have been granted to the Group.

Impairment of tangible assets

At the end of the reporting period, the Group reviews the carrying amounts of its property and equipment to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the relevant asset is estimated in order to determine the extent of the impairment loss (if any).

When it is not possible to estimate the recoverable amount of an asset individually, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs. When a reasonable and consistent basis of allocation can be identified, corporate assets are also allocated to individual cash-generating units, or otherwise they are allocated to the smallest group of cash-generating units for which a reasonable and consistent allocation basis can be identified.

Recoverable amount is the higher of fair value less costs of disposal and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset (or a cash-generating unit) for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset (or a cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or a cash-generating unit) is reduced to its recoverable amount. In allocating the impairment loss, the impairment loss is allocated first to reduce the carrying amount of any goodwill (if applicable) and then to the other assets on a pro-rata basis based on the carrying amount of each asset in the unit. The carrying amount of an asset is not reduced below the highest of its fair value less costs of disposal (if measurable), its value in use (if determinable) and zero. The amount of the impairment loss that would otherwise have been allocated to the asset is allocated pro rata to the other assets of the unit. An impairment loss is recognized immediately in profit or loss.

When an impairment loss subsequently reverses, the carrying amount of the asset (or cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset (or a cash-generating unit) in prior years. A reversal of an impairment loss is recognized immediately in profit or loss.

2. SIGNIFICANT ACCOUNTING POLICIES - continued

Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for services provided in the normal course of business, net of discounts and sales related taxes.

Revenue is recognized when the amount of revenue can be reliably measured; when it is probable that future economic benefits will flow to the Group and when specific criteria have been met for each of the Group's activities, as described below.

The Group's accounting policy for recognition of revenue from construction contracts is described in the accounting policy for construction contracts below.

Interest income is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount on initial recognition.

The Group's accounting policy for recognition of revenue from operating leases is described in the accounting policy for leasing below.

Construction contracts

Where the outcome of a construction contract can be estimated reliably, revenue and costs are recognized by reference to the stage of completion of the contract activity at the end of the reporting period, measured based on the proportion that contract costs incurred for work performed to date relative to the estimated total contract costs. Variations in contract work, claims and incentive payments are included to the extent that the amount can be measured reliably and its receipt is considered probable.

Where the outcome of a construction contract cannot be estimated reliably, contract revenue is recognized to the extent of contract costs incurred that it is probable will be recoverable. Contract costs are recognized as expenses in the period in which they are incurred.

When it is probable that total contract costs will exceed total contract revenue, the expected loss is recognized as an expense immediately in the statement of profit or loss.

Amounts billed for work performed but not yet paid by the customers are included in the consolidated statements of financial position under accounts receivable.

Unbilled revenue and deferred revenue

For all completed contracts and contracts in progress, when costs incurred plus recognized profits (less recognized losses) exceed progress billings, the surplus is shown as unbilled revenue under assets. For contracts in progress where progress billings exceed costs incurred plus recognized profits (less recognized losses), the surplus is shown as deferred revenue under liabilities.



2. SIGNIFICANT ACCOUNTING POLICIES - continued

Retirement benefits costs

Payments to defined contribution retirement benefit plans including state-managed retirement benefit schemes are recognized as an expense when employees have rendered service entitling them to the contributions.

Short-term employee benefits

Short-term employee benefits are recognised at the undiscounted amount of the benefits expected to be paid as and when employees rendered the services. All short-term employee benefits are recognised as an expense unless another IFRS requires or permits the inclusion of the benefit in the cost of an asset.

A liability is recognised for benefits accruing to employees (such as wages and salaries, annual leave and sick leave) after deducting any amount already paid.

Taxation

Income tax expense represents the sum of the tax currently payable and deferred tax.

The tax currently payable is based on taxable profit for the year. Taxable profit differs from 'profit before income taxes' as reported in the consolidated statements of profit or loss and other comprehensive income because of income or expense that are taxable or deductible in other years and items that are never taxable or deductible. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the end of the reporting period.

Deferred tax is recognized on temporary differences between the carrying amounts of assets and liabilities in the consolidated financial statements and the corresponding tax bases used in the computation of taxable profit. Deferred tax liabilities are generally recognized for all taxable temporary differences. Deferred tax assets are generally recognized for all deductible temporary differences to the extent that it is probable that taxable profits will be available against which those deductible temporary differences can be utilized. Such deferred tax assets and liabilities are not recognized if the temporary difference arises from the initial recognition of assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

Deferred tax liabilities are recognized for taxable temporary differences associated with investments in subsidiaries, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax assets arising from deductible temporary differences associated with such investments are only recognized to the extent that it is probable that there will be sufficient taxable profits against which to utilize the benefits of the temporary differences and they are expected to reverse in the foreseeable future.

The carrying amount of deferred tax assets is reviewed at the end of each reporting period and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

2. SIGNIFICANT ACCOUNTING POLICIES - continued

Taxation - continued

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset is realized, based on tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period.

The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Group expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Group intends to settle its current tax assets and liabilities on a net basis.

Current and deferred tax are recognized in profit or loss, except when they relate to items that are recognized in other comprehensive income or directly in equity, in which case, the current and deferred tax are also recognized in other comprehensive income or directly in equity respectively.

Foreign currencies

The individual financial statements of the China based subsidiaries (including the special purpose entity) are presented in the Chinese Renminbi ("RMB"), which is the currency of the primary economic environment in which they operate (their functional currency). The functional currency of the Company is the Canadian dollar ("CAD").

The consolidated financial statements of the Group are presented in United States Dollars ("US\$"), which the directors of the Company believe is a currency widely and commonly recognized in the global economy.

In preparing the financial statements of each individual group entity, transactions in currencies other than the functional currency of that entity (foreign currencies) are recognized at the rates of exchange prevailing on the dates of the transactions. At the end of the reporting period, monetary items denominated in foreign currencies are retranslated at the rates prevailing at that date. Non-monetary items carried at fair value that are denominated in foreign currencies are retranslated at the rates prevailing on the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

Exchange differences arising on the settlement of monetary items, and on the retranslation of monetary items, are recognized in profit or loss in the period in which they arise.

For the purposes of presenting consolidated financial statements, the assets and liabilities of the Group's foreign operations are translated into the presentation currency of the Group (i.e. US\$) using exchange rates prevailing at the end of each reporting period. Income and expense items are translated at the average exchange rates for the period, unless exchange rates fluctuate significantly during that period, in which case the exchange rates at the dates of the transactions are used. Exchange differences arising, if any, are recognized in other comprehensive income and accumulated in equity under the heading of foreign currency translation reserve.

2. SIGNIFICANT ACCOUNTING POLICIES - continued

Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale, are added to the cost of those assets until such time as the assets are substantially ready for their intended use or sale.

Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs eligible for capitalization.

All other borrowing costs are recognized in the statement of profit or loss in the period in which they are incurred.

Share-based compensation

Equity-settled share-based payments to employees and others providing similar services are measured at the fair value of the equity instruments at the grant date. Details regarding the determination of the fair value of equity-settled share-based transactions are set out in note 18.

The fair value of the equity-settled share-based payments determined at the grant date without taking into consideration all non-market vesting conditions is expensed on a graded vesting basis over the vesting period, based on the Group's estimate of equity instruments that will eventually vest, with a corresponding increase in equity (contributed surplus).

At the end of each reporting period, the Group revises its estimate of the number of equity instruments expected to vest based on assessment of all relevant non-market vesting conditions. The impact of the revision of the original estimates, if any, is recognized in profit or loss such that the cumulative expense reflects the revised estimate, with a corresponding adjustment to contributed surplus.

For share options that vest immediately at the date of grant, the fair value of the share options granted is expensed immediately to profit or loss.

When share options are exercised, the amount previously recognized in contributed surplus will be transferred to share capital. When the share options are forfeited after the vesting date or are still not exercised at the expiry date, the amount previously recognized in contributed surplus will be transferred to retained earnings.

Financial instruments

Financial assets and financial liabilities are recognized when a group entity becomes a party to the contractual provisions of the instruments.

Financial assets and financial liabilities are initially measured at fair value. Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities (other than financial assets or financial liabilities at fair value through profit or loss) are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at fair value through profit or loss are recognized immediately in profit or loss.

2. SIGNIFICANT ACCOUNTING POLICIES - continued

Financial instruments - continued

**Financial assets**

The Group's financial assets are classified as loans and receivables. The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition.

*Effective interest method*

The effective interest method is a method of calculating the amortized cost of a debt instrument and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees and points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the debt instrument, or, where appropriate, a shorter period, to the net carrying amount on initial recognition.

Income is recognized on an effective interest basis for debt instruments.

*Loans and receivables*

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Subsequent to initial recognition, loans and receivables (including unbilled revenue, deposits, accounts receivable, bank notes receivable, other receivables, amounts due from related parties, restricted cash and cash and cash equivalents) are measured at amortized cost using the effective interest method, less any impairment.

Interest income is recognized by applying the effective interest rate, except for short-term receivables where the recognition of interest would be immaterial.

*Impairment of financial assets*

Financial assets are assessed for indicators of impairment at the end of each reporting period. Financial assets are considered to be impaired when there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the financial assets have been affected.

Objective evidence of impairment could include:

- significant financial difficulty of the issuer or counterparty; or
- breach of contract, such as a default or delinquency in interest or principal payments; or
- it becoming probable that the borrower will enter bankruptcy or financial re-organization.

Objective evidence of impairment for a portfolio of receivables could include the Group's past experience of collecting payments, an increase in the number of delayed payments in the portfolio past the average credit period, observable changes in national or local economic conditions that correlate with default on receivables.

2. SIGNIFICANT ACCOUNTING POLICIES - continued

Financial instruments - continued

**Financial assets** - continued

*Impairment of financial assets* - continued

For financial assets carried at amortized cost, the amount of the impairment loss recognized is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the financial asset's original effective interest rate.

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of accounts receivable and unbilled revenue, where the carrying amount is reduced through the use of allowance accounts. Changes in the carrying amount of the allowance account are recognized in the statement of profit or loss. When an account receivable or unbilled revenue is considered uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited to the statement of profit or loss.

For financial assets measured at amortized cost, if, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed through the statement of profit or loss to the extent that the carrying amount of the investment at the date the impairment is reversed does not exceed what the amortized cost would have been had the impairment not been recognized.

**Financial liabilities and equity instruments**

*Classification as debt or equity*

Debt and equity instruments issued by a group entity are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangements and the definitions of a financial liability and an equity instrument.

*Equity instruments*

An equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities. Equity instruments issued by the Company are recognized at the proceeds received, net of direct issue costs.

*Convertible debentures*

The component parts of compound instruments (convertible debentures) issued by the Company are classified separately as financial liabilities and equity in accordance with the substance of the contractual arrangements and the definitions of a financial liability and an equity instrument.

2. SIGNIFICANT ACCOUNTING POLICIES - continued

Financial instruments - continued

**Financial liabilities and equity instruments** - continued

*Convertible debentures* - continued

Conversion option that will be settled by the exchange of a fixed amount of cash or another financial asset for a fixed number of the Company's own equity instruments is an equity instrument.

At the date of issue, the fair value of the liability component is estimated using the prevailing market interest rate for similar non-convertible instruments. This amount is recorded as a liability on an amortized cost basis using the effective interest method until extinguished upon conversion or at the instrument's maturity date.

The conversion option classified as equity is determined by deducting the amount of the liability component from the fair value of the compound instrument as a whole. This is recognized and included in equity, net of income tax effects, and is not subsequently remeasured. In addition, the conversion option classified as equity will remain in equity until the conversion option is exercised, in which case, the balance recognized in equity will be transferred to share capital. When the conversion option remains unexercised at the maturity date of the convertible note, the balance recognized in equity will be transferred to retained earnings. No gain or loss is recognized in the statement of profit or loss upon conversion or expiration of the conversion option.

Transaction costs that relate to the issue of the convertible notes are allocated to the liability and equity components in proportion to the allocation of the gross proceeds. Transaction costs relating to the equity component are recognized directly in equity. Transaction costs relating to the liability component are included in the carrying amount of the liability component and are amortized over the lives of the convertible notes using the effective interest method.

*Substantial modification of convertible debentures*

Modification is deemed to be substantial if the net present value of the cash flows under the modified terms, including any fees paid or received, is a least 10 percent different from the net present value of the remaining cash flows of the liability prior to the modification, both discounted at the original effective interest rate of the liability prior to the modification. A substantial modification of the terms of an existing financial liability is accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability.

The consideration paid, represented by the fair value of the modified convertible debentures are allocated to the liability and equity components of the original convertible debentures at the date of the extinguishment. The method used in allocating the consideration paid and transaction costs to the separate components of the original convertible debentures is consistent with that used in the original allocation to the separate components of the original convertible debentures of the proceeds received by the Company when the original convertible debentures were issued.

2. SIGNIFICANT ACCOUNTING POLICIES - continued

Financial instruments - continued

**Financial liabilities and equity instruments** - continued

*Convertible debentures* - continued

Once the allocation of the consideration is made, any resulting gain or loss is treated as follows:

- the amount of gain or loss relating to the original liability component is recognized in the statement of profit or loss; and
- the amount of consideration relating to the original equity component is recognized in equity in contributed surplus. The amount recognized in convertible debentures equity reserve attributable to the extinguished convertible debentures is also transferred to contributed surplus.

*Derivative financial instruments*

Derivatives are initially recognized at fair value at the date when derivative contracts are entered into and are subsequently remeasured to their fair value at the end of the reporting period. The resulting gain or loss is recognized in the statement of profit or loss immediately.

Derivatives embedded in non-derivative host contracts are treated as separate derivatives when they meet the definition of a derivative, their risks and characteristics are not closely related to those of the host contracts and the host contracts are not measured at fair value through profit or loss.

Generally, multiple embedded derivatives in a single instrument are treated as a single compound embedded derivative unless those derivatives related to different risk exposures and are readily separable and independent of each other.

Early redemption options embedded in convertible debentures are not closely related to the host contract unless:

- (i) the option's exercise price is approximately equal on each exercise date to the amortized cost of the host debt instrument; or
- (ii) the exercise price of a prepayment option reimburses the lender for an amount up to the approximate present value of lost interest for the remaining term of the host contract. The interest rate differential is the excess of the effective interest rate of the host contract over the effective interest rate the entity would receive at the prepayment date if it reinvested the principal amount prepaid in a similar contract for the remaining term of the host contract.

2. SIGNIFICANT ACCOUNTING POLICIES - continued

Financial instruments - continued

**Financial liabilities and equity instruments** - continued

*Financial liabilities at FVTPL*

Financial liabilities are classified as at FVTPL when the financial liability is designated as at FVTPL and upon initial recognition if:

- such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise; or
- the financial liability forms part of a group of financial assets or financial liabilities or both, which is managed and its performance is evaluated on a fair value basis, in accordance with the Group's documented risk management or investment strategy, and information about the grouping is provided internally on that basis; or
- it forms part of a contract containing one or more embedded derivatives, and IAS 39 permits the entire combined contract (asset or liability) to be designated as at FVTPL.

Financial liabilities at FVTPL are measured at fair value, with any gains or losses arising on remeasurement recognized in profit or loss. The net gain or loss recognized in the statement of profit or loss excludes any interest paid on the financial liabilities and is included in the loss on fair value changes of financial guarantee contracts. Fair value is determined in the manner described in note 29.

*Other financial liabilities*

Other financial liabilities (including borrowings, accounts and other payables, bank notes payable, other loans and convertible debentures) are subsequently measured at amortized cost using the effective interest method.

*Effective interest method*

The effective interest method is a method of calculating the amortized cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments (including all fees and points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial liability, or, where appropriate, a shorter period, to the net carrying amount on initial recognition. Interest expense is recognized on an effective interest basis.



2. SIGNIFICANT ACCOUNTING POLICIES - continued

Financial instruments - continued

**Financial liabilities and equity instruments** - continued

*Financial guarantee contracts*

A financial guarantee contract is a contract that requires the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payments when due in accordance with the terms of a debt instrument.

Financial guarantee contracts issued by the Group are initially measured at their fair values and designated as at fair value through profit or loss, and are subsequently measured at fair value.

**Derecognition**

The Group derecognizes a financial asset only when the contractual rights to the cash flows from the asset expire, or when it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity.

On derecognition of a financial asset in its entirety, the difference between the asset's carrying amount and the sum of the consideration received and receivable and the cumulative gain or loss that had been recognized in other comprehensive income and accumulated in equity is recognized in the statement of profit or loss.

The Group derecognizes financial liabilities when, and only when, the Group's obligations are discharged, cancelled or have expired. The difference between the carrying amount of the financial liability derecognized and the consideration paid and payable is recognized in the statement of profit or loss.

Leasing

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

**The Group as lessor**

Rental income from operating leases is recognized in profit or loss on a straight-line basis over the term of the relevant lease.

**The Group as lessee**

Operating lease payments are recognized as an expense on a straight-line basis over the lease term, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed.

2. SIGNIFICANT ACCOUNTING POLICIES - continued

Application of New and Revised IFRSs

*Amendments to IFRSs that are mandatorily effective for the current year*

The Group has applied the following amendments to IFRSs issued by the International Accounting Standards Board ("IASB") for the first time in the current year:

Amendments to IAS 7	Disclosure Initiative
Amendments to IAS 12	Recognition of Deferred Tax Assets for Unrealised Losses
Amendments to IFRS 12	As part of the Annual Improvements to IFRSs 2014 - 2016 Cycle

**Amendments to IAS 7 Disclosure Initiative**

The Group has applied these amendments for the first time in the current year. The amendments require an entity to provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both cash and non-cash changes. In addition, the amendments also require disclosures on changes in financial assets if cash flows from those financial assets were, or future cash flows will be, included in cash flows from financing activities.

Specifically, the amendments require the following to be disclosed: (i) changes from financing cash flows; (ii) changes arising from obtaining or losing control of subsidiaries or other businesses; (iii) the effect of changes in foreign exchange rates; (iv) changes in fair values; and (v) other changes.

A reconciliation between the opening and closing balances of these items is provided in note 30. Consistent with the transition provisions of the amendments, the Group has not disclosed comparative information for the prior year. Apart from the additional disclosure in note 30, the application of these amendments has had no impact on the Group's consolidated financial statements.

Except as described above, the application of the amendments to IFRSs in the current year has had no material impact on the Group's financial performance and positions for the current and prior years and/or on the disclosures set out in these consolidated financial statements.

2. SIGNIFICANT ACCOUNTING POLICIES - continued

Application of New and Revised IFRSs - continued

*New and revised IFRSs in issue but not yet effective*

The Group has not early applied the following new and revised IFRSs that have been issued but are not yet effective:

IFRS 9	Financial Instruments <sup>1</sup>
IFRS 15	Revenue from Contracts with Customers and the related Amendments <sup>1</sup>
IFRS 16	Leases <sup>2</sup>
IFRS 17	Insurance Contracts <sup>4</sup>
IFRIC 22	Foreign Currency Transactions and Advance Consideration <sup>1</sup>
IFRIC 23	Uncertainty over Income Tax Treatments <sup>2</sup>
Amendments to IFRS 2	Classification and Measurement of Share-based Payment Transactions <sup>1</sup>
Amendments to IFRS 4	Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts <sup>1</sup>
Amendments to IFRS 9	Prepayment Features with Negative Compensation <sup>2</sup>
Amendments to IFRS 10 and IAS 28	Sale or Contribution of Assets between an Investor and its Associate or Joint Venture <sup>3</sup>
Amendments to IAS 19	Plan Amendment, Curtailment or Settlement <sup>2</sup>
Amendments to IAS 28	Long-term Interests in Associates and Joint Ventures <sup>2</sup>
Amendments to IAS 40	Transfers of Investment Property <sup>1</sup>
Amendments to IAS 28	As part of the Annual Improvements to IFRSs 2014 - 2016 Cycle <sup>1</sup>
Amendments to IFRSs	Annual Improvements to IFRSs 2015 - 2017 Cycle <sup>2</sup>

<sup>1</sup> Effective for annual periods beginning on or after January 1, 2018

<sup>2</sup> Effective for annual periods beginning on or after January 1, 2019

<sup>3</sup> Effective for annual periods beginning on or after a date to be determined

<sup>4</sup> Effective for annual periods beginning on or after January 1, 2021

2. SIGNIFICANT ACCOUNTING POLICIES - continued

Application of New and Revised IFRSs - continued

**IFRS 9 *Financial Instruments***

IFRS 9 introduces new requirements for the classification and measurement of financial assets, financial liabilities, general accounting and impairments for financial assets.

Key requirements of IFRS 9 which are relevant to the Group are:

- All recognized financial assets that are within the scope of IFRS 9 are required to be subsequently measured at amortized cost or fair value. Specifically, debt investments that are held within a business model whose objective is to collect the contractual cash flows, and that have contractual cash flows that are solely payments of principal and interest on the principal outstanding are generally measured at amortized cost at the end of subsequent accounting periods. Debt instruments that are held within a business model whose objective is achieved both by collecting contractual cash flows and selling financial assets, and that have contractual terms that give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding, are generally measured at fair value through other comprehensive income. All other financial assets are measured at their fair value at subsequent accounting periods. In addition, under IFRS 9, entities may make an irrevocable election to present subsequent changes in the fair value of an equity investment (that is not held for trading) in other comprehensive income, with only dividend income generally recognized in the statement of profit or loss.
- With regard to the measurement of financial liabilities designated as at fair value through profit or loss, IFRS 9 requires that the amount of change in the fair value of the financial liability that is attributable to changes in the credit risk of that liability is presented in other comprehensive income, unless the recognition of the effects of changes in the liability's credit risk in other comprehensive income would create or enlarge an accounting mismatch in profit or loss. Changes in fair value attributable to a financial liability's credit risk are not subsequently reclassified to profit or loss. Under IAS 39 *Financial Instruments: Recognition and Measurement*, the entire amount of the change in the fair value of the financial liability designated as fair value through profit or loss is presented in profit or loss.
- In relation to the impairment of financial assets, IFRS 9 requires an expected credit loss model, as opposed to an incurred credit loss model under IAS 39. The expected credit loss model requires an entity to account for expected credit losses and changes in those expected credit losses at each reporting date to reflect changes in credit risk since initial recognition. In other words, it is no longer necessary for a credit event to have occurred before credit losses are recognized.

Application of New and Revised IFRSs - continued

**IFRS 9 *Financial Instruments*** - continued

Based on the Group's financial instruments and risk management policies as at June 30, 2018, the management of the Company anticipates the following potential impact on initial application of IFRS 9:

*Classification and measurement*

All financial assets and financial liabilities will continue to be measured on the same bases as are currently measured under IAS 39.

*Impairment*

In general, the management of the Company anticipates that the application of the expected credit loss model of IFRS 9 will result in earlier provision of credit losses which are not yet incurred in relation to the Group's financial assets measured at amortised cost and other items that subject to the impairment provisions upon application of IFRS 9 by the Group.

Based on the assessment by the management of the Company, if the expected credit loss model were to be applied by the Group, the accumulated amount of impairment loss to be recognised by the Group as at July 1, 2018 would be increased as compared to the accumulated amount recognized under IAS 39 mainly attributable to expected credit losses provision on accounts receivable and unbilled revenue. Such further impairment recognised under expected credit loss model would reduce the opening retained earnings and increase the deferred tax assets at July 1, 2018.

2. SIGNIFICANT ACCOUNTING POLICIES - continued

Application of New and Revised IFRSs - continued

**IFRS 15 Revenue from Contracts with Customers**

IFRS 15 was issued which establishes a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. IFRS 15 will supersede the current revenue recognition guidance including IAS 18 *Revenue*, IAS 11 *Construction Contracts* and the related Interpretations when it becomes effective.

The core principle of IFRS 15 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Specifically, the Standard introduces a 5-step approach to revenue recognition:

- Step 1: Identify the contract(s) with a customer;
- Step 2: Identify the performance obligations in the contract;
- Step 3: Determine the transaction price;
- Step 4: Allocate the transaction price to the performance obligations in the contract; and
- Step 5: Recognize revenue when (or as) the entity satisfies a performance obligation.

Under IFRS 15, an entity recognizes revenue when (or as) a performance obligation is satisfied, i.e. when 'control' of the goods or services underlying the particular performance obligation is transferred to the customer. Far more prescriptive guidance has been added in IFRS 15 to deal with specific scenarios. Furthermore, extensive disclosures are required by IFRS 15.

In 2016, the IASB issued Clarifications to IFRS 15 in relation to the identification of performance obligations, principal versus agent considerations, as well as licensing application guidance.

The management of the Company anticipates that the application of IFRS 15 in the future may result in more disclosures, however, the management of the Company does not anticipate that the application of IFRS 15 will have a material impact on the timing and amounts of revenue recognized in the respective reporting periods.

2. SIGNIFICANT ACCOUNTING POLICIES - continued

Application of New and Revised IFRSs - continued

**IFRS 16 Leases**

IFRS 16 introduces a comprehensive model for the identification of lease arrangements and accounting treatments for both lessors and lessees. IFRS 16 will supersede IAS 17 *Leases* and the related interpretations when it becomes effective.

IFRS 16 distinguishes lease and service contracts on the basis of whether an identified asset is controlled by a customer. Distinctions of operating leases and finance leases are removed for lessee accounting, and is replaced by a model where a right-of-use asset and a corresponding liability have to be recognized for all leases by lessees, except for short-term leases and leases of low value assets.

The right-of-use asset is initially measured at cost and subsequently measured at cost (subject to certain exceptions) less accumulated depreciation and impairment losses, adjusted for any remeasurement of the lease liability. The lease liability is initially measured at the present value of the lease payments that are not paid at that date. Subsequently, the lease liability is adjusted for interest and lease payments, as well as the impact of lease modifications, amongst others. For the classification of cash flows, the Group currently presents upfront prepaid lease payments as investing cash flows in relation to leasehold lands for owned use and those classified as investment properties while other operating lease payments are presented as operating cash flows. Upon application of IFRS 16, lease payments in relation to lease liability will be allocated into a principal and an interest portion which will be presented as financing cash flows by the Group.

Under IAS 17, the Group has already recognized an asset for prepaid lease payments for leasehold lands where the Group is a lessee. The application of IFRS 16 may result in potential changes in classification of these assets depending on whether the Group presents right-of-use assets separately or within the same line item at which the corresponding underlying assets would be presented if they were owned.

In contrast to lessee accounting, IFRS 16 substantially carries forward the lessor accounting requirements in IAS 17, and continues to require a lessor to classify a lease either as an operating lease or a finance lease.

Furthermore, extensive disclosures are required by IFRS 16.

As at June 30, 2018, the Group has non-cancellable operating lease commitments of US\$2,074,196 as disclosed in note 27. A preliminary assessment indicates that these arrangements will meet the definition of a lease. Upon application of IFRS 16, the Group will recognize a right-of-use asset and a corresponding liability in respect of all these leases unless they qualify for low value or short-term leases.

2. SIGNIFICANT ACCOUNTING POLICIES - continued

Application of New and Revised IFRSs - continued

**IFRS 16 Leases** - continued

In addition, the Group currently considers refundable rental deposits paid of US\$37,762 and refundable rental deposits received of US\$16,587 as rights and obligations under leases to which IAS 17 applies. Based on the definition of lease payments under IFRS 16, such deposits are not payments relating to the right to use the underlying assets, accordingly, the carrying amounts of such deposits may be adjusted to amortised cost and such adjustments are considered as additional lease payments. Adjustments to refundable rental deposits paid would be included in the carrying amount of right-of-use assets. Adjustments to refundable rental deposits received would be considered as advance lease payments.

Furthermore, the application of new requirements may result in changes in measurement, presentation and disclosure as indicated above.

Except as described above, the management of the Company anticipates that the application of other new and amendments to IFRSs and Interpretations will have no material impact on the consolidated financial statements in the foreseeable future.

3. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY

In the application of the Group's accounting policies, which are described in note 2, management is required to make judgements, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

***Critical judgements in applying accounting policies***

The following are the critical judgements, apart from those involving estimations (see below), that management has made in the process of applying the Group's accounting policies and that have the most significant effect on the amounts recognized in the consolidated financial statements.

Control over Zhejiang Boyuan Construction Co., Ltd. ("Zhejiang Boyuan")

In order to comply with PRC laws and regulations limiting foreign ownership of or imposing conditions on holding National Class I Construction Qualification in the PRC, the Group operates its business through Zhejiang Boyuan by means of Contractual Arrangement (as defined below).



3. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION  
UNCERTAINTY - continued

*Critical judgements in applying accounting policies* - continued

Control over Zhejiang Boyuan Construction Co., Ltd. ("Zhejiang Boyuan") - continued

Management of the Company assessed whether or not the Group has control over Zhejiang Boyuan based on whether the Group has the practical ability to direct the relevant activities of Zhejiang Boyuan unilaterally. In making their judgment, the management of the Company considered the Contractual Arrangement (as defined below).

On January 10, 2009, Zhejiang Jianyou Trading Co., Ltd. ("China Privco"), a wholly-owned PRC subsidiary of the Company, Zhejiang Boyuan and shareholders of Zhejiang Boyuan, entered into a series of agreements (the "Contractual Arrangement"). Mr. Shou Cailiang ("Mr. Shou"), the ultimate controlling shareholder, CEO and director of the Company, holds 90% equity interest in Zhejiang Boyuan.

The key provisions of the Contractual Arrangement are follows:

- (i) *Exclusive Option Agreement:* China Privco can acquire the equity interest in, and all or part of the assets and business of, Zhejiang Boyuan at any time if legally permitted at a minimal amount;
- (ii) *Management Agreement:* Zhejiang Boyuan entrusted China Privco to manage and operate the business of Zhejiang Boyuan. China Privco will be remunerated with the net earnings before tax of Zhejiang Boyuan and will assume all operational risks and bear all losses of Zhejiang Boyuan;
- (iii) *Shareholder's Voting Proxy Agreement:* The shareholders of Zhejiang Boyuan granted the right to exercise all of the voting rights of Zhejiang Boyuan to China Privco; and
- (iv) *Share Pledged Agreement:* The shareholders of Zhejiang Boyuan pledged all of the shares of Zhejiang Boyuan they own to China Privco to guarantee their obligations under Exclusive Option Agreement, Management Agreement and Shareholder's Voting Proxy Agreement.

Management of the Company, after consulting legal opinion, are of the view that the terms of the Contractual Arrangement have in substance enabled China Privco to have power over Zhejiang Boyuan, rights to variable returns from its involvement with Zhejiang Boyuan, and has the ability to use its power to affect its returns, despite the absence of formal legal equity interests held by the Group therein. Accordingly, Zhejiang Boyuan is accounted for as a consolidated structured entity and as a subsidiary of the Company.

In the opinion of the management of the Company, with reference to opinion of legal counsel, the Contractual Arrangement is in compliance with existing PRC laws and regulations, are valid, binding and enforceable, and do not result in any violation of PRC laws or regulations currently in effect in all material respects. However, uncertainties in the PRC legal system could cause the Group's current contractual arrangement structure to be found in violation of any existing and/or future PRC laws or regulations and could limit the Company's ability, through China Privco, to enforce its rights under the Contractual Arrangement.

3. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION  
UNCERTAINTY - continued

*Critical judgements in applying accounting policies* - continued

Control over Zhejiang Boyuan Construction Co., Ltd. ("Zhejiang Boyuan") - continued

Substantially all of the operations of the Group is carried out through Zhejiang Boyuan. If the current structure or any of the Contractual Arrangement were found to be in violation of any existing or future PRC law, the Group may be subject to penalties, which may include but not be limited to, the cancellation or revocation of the Group's business and operating licenses, being required to restructure the Group's operations or discontinue the Group's operating activities. The imposition of any of these or other penalties may result in a material and adverse effect on the Group's ability to conduct its operations. In such case, the Group may not be able to operate or control Zhejiang Boyuan, which may result in its deconsolidation.

*Key sources of estimation uncertainty*

The following are the key assumptions concerning the future, and other key sources of estimation uncertainty at the end of the reporting period that may have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

Construction contracts

Revenue recognition on a project is dependent on management's estimation of the total outcome of the construction contract, as well as the work done to date. The Group reviews and revises the estimates of contract revenue, contract costs, variation orders and contract claims prepared for each construction contract as the contract progresses. Budgeted construction revenue is determined in accordance with the terms set out in the relevant contracts. Budgeted construction costs are prepared by the management on the basis of quotations from time to time provided by the suppliers or vendors involved and the experience of the management. In order to keep the budget accurate and up-to-date, the management conducts periodic reviews of the management budgets by comparing the budgeted amounts to the actual amounts incurred. Construction revenue, construction costs and unbilled revenue include amounts derived using the percentage of completion method applied to construction contracts. Percentage of completion is calculated based on the costs incurred on each construction contract at the end of the respective accounting period divided by the total estimated costs for the contract and then multiplied by the estimated construction revenue expected to be earned.

A considerable amount of judgement is required in estimating the total contract revenue, contract costs, variation orders and contract claims which may have an impact in terms of percentage of completion and profit recognized for each job.

Impairment of accounts receivable and unbilled revenue

On assessing any impairment of the Group's accounts receivable and unbilled revenue, management regularly reviews the recoverability, creditworthiness of customers and ages of accounts receivable and unbilled revenue. Impairment on accounts receivable and unbilled revenue is made based on estimation of the future cash flows discounted at the original effective interest rates. If the financial condition of the customers of the Group deteriorates, resulting in an impairment of their ability to make payments, additional impairment may be required. As at June 30, 2018, the carrying amount of accounts receivable and unbilled revenue are approximately US\$70,312,000 (June 30, 2017: US\$63,915,000) (net of allowance for doubtful debts of approximately US\$9,108,000 (June 30, 2017: US\$4,123,000)) and US\$139,783,000, (June 30, 2017: US\$116,433,000) (net of allowance for doubtful debts of approximately US\$16,035,000 (June 30, 2017: US\$13,948,000)), respectively.

## BOYUAN CONSTRUCTION GROUP, INC.

### 3. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY - continued

#### *Key sources of estimation uncertainty* - continued

#### Expected timing of collections of accounts receivable and unbilled revenue

The Group classifies its accounts receivable and unbilled revenue as current and non-current assets based on the expected timing of collections of cash. This determination requires significant judgement and is based on the characteristics of each customer, contract terms and past repayment record.

### 4. PROPERTY AND EQUIPMENT

Movements in the carrying value of property and equipment were as follows:

	<u>Buildings</u>	<u>Machinery, equipment and scaffoldings</u>	<u>Vehicles</u>	<u>Office equipment</u>	<u>Leasehold improvements</u>	<u>Construction in progress</u>	<u>Total</u>
	US\$	US\$	US\$	US\$	US\$	US\$	US\$
<b>COST</b>							
Balance at June 30, 2016	5,447,359	20,482,154	1,847,704	1,808,156	1,538,428	484,521	31,608,322
Additions	-	206,146	137,346	82,874	-	267,067	693,433
Transfer	-	-	-	24,673	663,579	(688,252)	-
Disposals	-	(63,129)	(426,112)	(29,544)	-	-	(518,785)
Effect of foreign currency exchange differences	(107,308)	(402,755)	(37,868)	(35,225)	(26,929)	(11,690)	(621,775)
Balance at June 30, 2017	5,340,051	20,222,416	1,521,070	1,850,934	2,175,078	51,646	31,161,195
Additions	-	323,368	32,158	116,618	-	99,673	571,817
Disposals	-	-	(58,867)	(13,425)	-	-	(72,292)
Effect of foreign currency exchange differences	126,171	472,280	36,396	41,967	51,391	(484)	727,721
Balance at June 30, 2018	5,466,222	21,018,064	1,530,757	1,996,094	2,226,469	150,835	32,388,441
<b>ACCUMULATED DEPRECIATION</b>							
Balance at June 30, 2016	2,335,836	16,734,667	1,549,185	1,427,163	1,461,508	-	23,508,359
Depreciation expense	143,055	1,502,141	88,916	145,949	252,803	-	2,132,864
Disposals	-	(35,459)	(343,752)	(26,881)	-	-	(406,092)
Effect of foreign currency exchange differences	(45,287)	(322,194)	(31,815)	(27,508)	(27,505)	-	(454,309)
Balance at June 30, 2017	2,433,604	17,879,155	1,262,534	1,518,723	1,686,806	-	24,780,822
Depreciation expense	143,104	982,611	69,718	142,892	231,528	-	1,569,853
Disposals	-	-	(55,924)	(12,754)	-	-	(68,678)
Effect of foreign currency exchange differences	55,054	405,650	29,595	33,660	35,898	-	559,857
Balance at June 30, 2018	2,631,762	19,267,416	1,305,923	1,682,521	1,954,232	-	26,841,854
<b>NET BOOK AMOUNTS</b>							
At June 30, 2017	2,906,447	2,343,261	258,536	332,211	488,272	51,646	6,380,373
At June 30, 2018	2,834,460	1,750,648	224,834	313,573	272,237	150,835	5,546,587

Buildings with a carrying amount of US\$2,436,171 (June 30, 2017: US\$2,473,519) have been pledged to secure the borrowings as disclosed in note 12.

## BOYUAN CONSTRUCTION GROUP, INC.

### 5. PREPAID LEASE PAYMENTS

	<u>2018</u> US\$	<u>2017</u> US\$
The Group's prepaid lease payments comprise:		
Leasehold land in the PRC:		
Medium-term leases	88,170	90,546
Analyzed for reporting purposes as:		
Non-current assets	85,763	85,509
Current assets	2,407	5,037
	<u>88,170</u>	<u>90,546</u>

In June 2007, Zhejiang Boyuan acquired a 50 year land use right in Jiaxing, Zhejiang, in the PRC for the construction of an office building and 2 residential buildings used by the Group as employee residence. The right will expire on August 23, 2056.

Prepaid lease payments with a carrying amount of US\$88,170 (June 30, 2017: US\$90,546) have been pledged to secure the borrowings as disclosed in note 12.

### 6. UNBILLED REVENUE

Unbilled revenue comprises gross amount due from customers for completed contracts and contracts in progress. Unbilled revenue is the net amount of construction costs incurred plus recognized profit less recognized losses and progress billings.

	<u>2018</u> US\$	<u>2017</u> US\$
Completed contracts	60,081,408	91,496,534
Contracts in progress	98,350,323	43,101,084
Gross unbilled revenue	158,431,731	134,597,618
Less: Effect of discounting, net	(2,613,692)	(4,216,631)
Allowance for doubtful debts	(16,034,952)	(13,947,881)
	<u>139,783,087</u>	<u>116,433,106</u>
Analyzed for reporting purposes as:		
Non-current assets	28,853,451	32,076,872
Current assets	110,929,636	84,356,234
	<u>139,783,087</u>	<u>116,433,106</u>

The non-current unbilled revenue is measured at amortized cost using interest rate of 8.79% (June 30, 2017: 9.74%) per annum.

BOYUAN CONSTRUCTION GROUP, INC.

6. UNBILLED REVENUE - continued

The unbilled revenue recognized for contracts in progress included in the unbilled revenue are as follows:

	<u>2018</u> US\$	<u>2017</u> US\$
Aggregate costs of construction	386,111,250	163,562,922
Gross profit recognized	<u>52,838,343</u>	<u>22,435,597</u>
	438,949,593	185,998,519
Less: aggregate of progress billings	<u>(340,599,270)</u>	<u>(142,897,435)</u>
Contracts in progress - unbilled revenue portion, end of year	<u><u>98,350,323</u></u>	<u><u>43,101,084</u></u>

Unbilled revenue for completed contracts included the following amounts of unbilled retention monies which are analyzed as follows:

	<u>2018</u> US\$	<u>2017</u> US\$
Expected to be due within one year	-	-
Expected to be due after one year	<u>-</u>	<u>336,565</u>
	<u><u>-</u></u>	<u><u>336,565</u></u>

During the year ended June 30, 2018, construction revenue of US\$268,052,393 (June 30, 2017: US\$119,920,096) generated from contracts in progress were recognized in the statement of profit or loss.

Included in the Group's unbilled revenue are debtors with aggregate carrying amount of approximately US\$19,633,000 (June 30, 2017: US\$17,014,000) which are past due based on the payment terms stated in each construction contract as at the reporting date for which the Group has not provided for impairment loss. Management of the Company are of the opinion that there has not been a significant change in credit quality and balances are still considered fully recoverable due to the long-term/ on-going relationship and good repayment record from these customers. The Group does not hold collateral over these balances.

Aging of unbilled revenue which are past due but not impaired

	<u>2018</u> US\$	<u>2017</u> US\$
0 - 180 days	19,632,753	16,268,421
1 - 2 years	<u>-</u>	<u>745,775</u>
	<u><u>19,632,753</u></u>	<u><u>17,014,196</u></u>

BOYUAN CONSTRUCTION GROUP, INC.

6. UNBILLED REVENUE - continued

Movement in allowance for doubtful debts

	<u>2018</u> US\$	<u>2017</u> US\$
At beginning of the year	13,947,881	15,382,650
Impairment losses recognized	5,069,917	2,036,981
Impairment losses reversed	(3,281,850)	(3,162,991)
Effect of foreign currency exchange differences	299,004	(308,759)
At end of the year	<u>16,034,952</u>	<u>13,947,881</u>

Recoverability of unbilled revenue is reviewed on a case-by-case basis when there is objective evidence that a customer will default. Management takes into consideration the customer's payment history, the credit worthiness and the current economic environment in which the customer operates to assess the amount of impairment.

As at June 30, 2018, the Group identified unbilled revenue of US\$16,034,952 (June 30, 2017: US\$13,947,881) that were impaired due to difficulties and delay in collecting the outstanding balances.

7. ACCOUNTS RECEIVABLE/BANK NOTES RECEIVABLE

(a) Accounts receivable

	<u>2018</u> US\$	<u>2017</u> US\$
Accounts receivable	82,141,991	70,638,719
Less: Effect of discounting, net	(2,722,529)	(2,601,361)
Allowance for doubtful debts	(9,107,679)	(4,122,672)
	<u>70,311,783</u>	<u>63,914,686</u>
Analyzed for reporting purpose as:		
Non-current assets	20,413,009	15,488,246
Current assets	49,898,774	48,426,440
	<u>70,311,783</u>	<u>63,914,686</u>

The non-current accounts receivable is measured at amortized cost using interest rate of 8.79% (June 30, 2017: 9.74%) per annum.

BOYUAN CONSTRUCTION GROUP, INC.

7. ACCOUNTS RECEIVABLE/BANK NOTES RECEIVABLE - continued

(a) Accounts receivable - continued

Retention receivable included in accounts receivable is analyzed as follows:

	<u>2018</u> US\$	<u>2017</u> US\$
Due within one year	1,566,355	2,739,719
Due after one year	3,915,659	16,654
	<u>5,482,014</u>	<u>2,756,373</u>

Due dates of accounts receivable are determined based on the agreed payment dates as stipulated in the contracts.

The Group will assess the potential customer's credit quality and defines credit limits by customer. In addition, the Group will review the repayment history of receivables by each customer with reference to the payment terms stated in the contracts, the credit worthiness and the current economic environment in which the customer operates to assess the recoverability of accounts receivable.

Included in the Group's accounts receivable balance are debtors with an aggregate carrying amount of approximately US\$22,114,000 (June 30, 2017: US\$17,000,000) which are past due based on the payment terms stated in each construction contract as at the reporting date for which the Group has not provided for impairment loss. Management of the Company are of the opinion that there has not been a significant change in credit quality and balances are still considered fully recoverable due to the long-term/ on-going relationship and good repayment record from these customers. The Group does not hold any collateral over these balances.

Aging of accounts receivable which are past due but not impaired

	<u>2018</u> US\$	<u>2017</u> US\$
0 - 180 days	18,665,794	10,983,150
181 - 365 days	1,854,179	6,017,347
1 - 2 years	1,594,215	-
	<u>22,114,188</u>	<u>17,000,497</u>

BOYUAN CONSTRUCTION GROUP, INC.

7. ACCOUNTS RECEIVABLE/BANK NOTES RECEIVABLE - continued

(a) Accounts receivable - continued

Movement in the allowance for doubtful debts

	<u>2018</u> US\$	<u>2017</u> US\$
At beginning of the year	4,122,672	1,099,808
Impairment losses recognized	5,909,710	3,110,623
Impairment losses reversed	(937,150)	(81,514)
Effect of foreign currency exchange differences	12,447	(6,245)
At end of the year	<u>9,107,679</u>	<u>4,122,672</u>

(b) Bank notes receivable

The bank notes receivable of the Group is of the age within one year at the end of the reporting period. As at June 30, 2018, approximately US\$9,400,000 (June 30, 2017: Nil) was discounted to banks and a financial institution for cash proceeds with recourse. If these bank notes receivable were not paid at maturity, the banks and the financial institution have the right to request the Group to pay the unsettled balance.

8. DEPOSITS

	<u>2018</u> US\$	<u>2017</u> US\$
Contract performance deposits (Note a)	10,800,825	8,300,677
Project tender deposits (Note b)	2,060,275	1,866,633
Others	846,547	133,451
	<u>13,707,647</u>	<u>10,300,761</u>

Notes:

- (a) Contract performance deposits are advanced to customers at the beginning of construction projects. The deposits are repaid to the Group based on the progress of construction and terms of the contract. During the year ended June 30, 2018, a reversal of impairment loss of US\$691,525 was credited to statement of profit or loss (June 30, 2017: a provision of impairment loss of US\$587,251).

As at June 30, 2018, contract performance deposits amounted to US\$5,670,214 (June 30, 2017: US\$194,328) are expected to be recovered or settled in more than twelve months from the end of the reporting period.

- (b) Project tender deposits are advanced to potential customers during the contract tendering period. The deposits are repaid to the Group when the tendering process is completed.



## BOYUAN CONSTRUCTION GROUP, INC.

### 9. ADVANCES AND PREPAID EXPENSES

	<u>2018</u> US\$	<u>2017</u> US\$
Advances to project managers and suppliers (Note)	6,142,765	1,407,335
Prepaid expenses	58,908	44,268
Others	533,507	306,875
	<u>6,735,180</u>	<u>1,758,478</u>

Note: The Group advanced monies to suppliers and project managers in order to secure construction materials and services. The advances of US\$6,128,772 (June 30, 2017: US\$1,219,042) to the project managers are held in bank accounts in trust for the Group. The advances are expected to be fully utilized in various construction projects within six months from the end of the reporting period.

### 10. RELATED PARTY BALANCES AND TRANSACTIONS

The Group has the following related party balances:

	<u>2018</u> US\$	<u>2017</u> US\$
Due from a company controlled by Mr. Shou	56,441	55,139
Due from shareholders (Note)	755,233	-
	<u>811,674</u>	<u>55,139</u>

Note: Balance represented cash advanced to the shareholders, for placement into a bank to secure a bank loan granted to the Group during the current year.

The balances are non-operating nature, unsecured, interest-free and repayable on demand. The Group also had guarantees provided by related parties at the end of the reporting period shown in note 12.

#### **Related party transactions**

##### *Key management personnel compensation*

Key management personnel include all directors, chief executive officer, chief financial officer, corporate secretary and vice president. The remuneration of key management personnel for the year was as follows:

	<u>2018</u> US\$	<u>2017</u> US\$
Salaries, bonus and other short-term employee benefits	349,361	345,086
Contributions to retirement benefit scheme	9,099	8,889
	<u>358,460</u>	<u>353,975</u>

BOYUAN CONSTRUCTION GROUP, INC.

11. RESTRICTED CASH/BANK NOTES PAYABLE/CASH AND CASH EQUIVALENTS

(a) Restricted cash/bank notes payable

As at June 30, 2018 and 2017, the Group had restricted cash pledged for credit facilities as follows:

	<u>2018</u> US\$	<u>2017</u> US\$
Bank notes payable deposits	5,336,476	2,287,624
Bank loans deposits	<u>3,209,739</u>	<u>4,537,473</u>
	<u>8,546,215</u>	<u>6,825,097</u>

The restricted cash carries interest at market rates ranging from 1.15% to 1.95% (June 30, 2017: 1.55% to 1.80%) per annum.

A bank note payable is a note issued by a bank for payments in future, which defers the payment until the due date for redeeming the note. The bank notes payable carry interest at variable-rates at 1.4% to 2.1% (June 30, 2017: 1.3% to 2.0%) per annum. According to the bank notes payable agreement with the banks, a certain percentage of the payable amount is required to be deposited at the banks as security for bank notes payable of the Group amounted to approximately US\$16,114,000 as of June 30, 2018 (June 30, 2017: US\$6,456,000). Related parties (includes Mr. Shou and his family member) and some independent third parties have provided guarantees for bank notes payable of the Group amounted to US\$8,307,000 as of June 30, 2018 (June 30, 2017: US\$4,427,000). The restrictions on the deposited cash will be released between July 2018 and December 2018, when the bank notes payable mature.

The restricted cash of deposits for bank loans varies based on the bank's credit policy and can only be withdrawn when the loans mature.

(b) Cash and cash equivalents

Cash at banks carries interest at market rates which range from 0.03% to 1.10% (June 30, 2017: 0.01% to 1.10%) per annum.

BOYUAN CONSTRUCTION GROUP, INC.

12. BORROWINGS

As at June 30, 2018, the Group has borrowings outstanding totaling US\$75,299,783 (June 30, 2017: US\$66,776,845) for working capital purpose.

	<u>2018</u> US\$	<u>2017</u> US\$
Bank loans	65,900,106	66,776,845
Advance from banks and a financial institution on discounted bank notes receivable with recourse - repayable within one year (Note a)	<u>9,399,677</u>	<u>-</u>
	<u>75,299,783</u>	<u>66,776,845</u>
Secured	65,900,106	61,348,109
Unsecured	<u>9,399,677</u>	<u>5,428,736</u>
	<u>75,299,783</u>	<u>66,776,845</u>

Note:

- (a) Balance represented bank notes receivable discounted to banks and a financial institution as at June 30, 2018 for cash proceeds with recourse of approximately US\$9,400,000 (June 30, 2017: Nil). If the bank notes receivable are not paid at maturity, the banks and the financial institution have the right to request the Group to pay the unsettled balance.

## BOYUAN CONSTRUCTION GROUP, INC.

### 12. BORROWINGS - continued

As at June 30, 2018 and 2017, a wholly-owned subsidiary, related parties (includes Mr. Shou and his family member) and some independent third parties have provided guarantees to certain banks and a financial institution over borrowings granted to the Group that amounted to approximately US\$8,610,000, US\$11,712,000 and US\$39,242,000 (June 30, 2017: US\$8,854,000, US\$15,073,000 and US\$30,692,000), respectively. In addition, the Group has pledged its assets to secure bank loans of US\$6,336,000 (June 30, 2017: US\$6,729,000) granted to the Group and the carrying values of the pledged assets are as follows:

	<u>2018</u> US\$	<u>2017</u> US\$
Restricted cash	3,209,739	4,537,473
Property and equipment	2,436,171	2,473,519
Prepaid lease payments	88,170	90,546
	<u>5,734,080</u>	<u>7,101,538</u>

The ranges of effective interest rates (which are also equal to contractual interest rates) on the Group's borrowings and their carrying values are as follow:

	<u>2018</u> US\$	<u>2017</u> US\$
Fixed-rate borrowings		
Denominated in RMB (range from 4.35% to 15.00% per annum as of June 30, 2018 and range from 4.35% to 8.70% per annum as of June 30, 2017)	25,629,630	34,018,504
Variable rate borrowings		
Denominated in RMB (range from 4.57% to 7.00% per annum as of June 30, 2018 and range from 4.40% to 9.60% per annum as of June 30, 2017) (Note a)	49,670,153	32,758,341
	<u>75,299,783</u>	<u>66,776,845</u>

Note:

- (a) For borrowings in RMB, the variable rates range from Prime plus 0.27% to Prime times 1.61% per annum as of June 30, 2018 (June 30, 2017: ranged from Prime plus 0.05% to Prime plus 5.25% per annum). Prime is the benchmark rate of the People's Bank of China.

BOYUAN CONSTRUCTION GROUP, INC.

13. ACCOUNTS AND OTHER PAYABLES AND ACCRUED LIABILITIES

	<u>2018</u> US\$	<u>2017</u> US\$
Accounts payable (Note a)	5,399,194	3,237,024
Trade accruals	22,881,391	4,867,234
Salaries and wages payable	328,388	326,189
Other taxes payable	15,395,945	8,173,430
Contract performance deposits from sub-contractors (Note b)	4,307,595	2,983,466
Project tender deposits from sub-contractors	1,634,475	1,619,932
Others	1,097,478	788,082
	<u>51,044,466</u>	<u>21,995,357</u>

Notes:

- (a) The accounts payable are trade in nature and the average credit period on purchase of goods ranges from 30 to 90 days. The Group has financial risk management policies in place to ensure that payables are settled within the credit timeframe.
- (b) Contract performance deposits amounted to US\$3,812,575 (June 30, 2017: US\$1,667,787) as at June 30, 2018 are expected to be paid or settled in more than twelve months from the end of the reporting period.

14. OTHER LOANS

As at June 30, 2018, the Group has outstanding unsecured other loans totaling US\$643,698 (June 30, 2017: US\$3,778,113) for working capital and capital expenditure purposes.

	<u>2018</u> US\$	<u>2017</u> US\$
Loans from third parties (Note a)	633,465	3,750,978
Obligation under a finance lease (Note b)	10,233	27,135
	<u>643,698</u>	<u>3,778,113</u>
Carrying amount repayable:		
Within one year	643,698	3,769,693
After one year	-	8,420
	<u>643,698</u>	<u>3,778,113</u>
Less: Amounts shown under current liabilities	<u>(643,698)</u>	<u>(3,769,693)</u>
	<u>-</u>	<u>8,420</u>

Notes:

- (a) For the years ended June 30, 2018 and 2017, the Group obtained several loans from independent third parties. The loans were unsecured, interest-free and repayable within one year from the end of the reporting period.
- (b) For the year ended June 30, 2017, the Group entered into the finance lease arrangement to lease a motor vehicle, with a lease period of two years ending on December 31, 2018. As at June 30, 2018, US\$10,233 (June 30, 2017: US\$27,135) will be repayable within one year and Nil (June 30, 2017: US\$8,420) will be repayable after one year.

## BOYUAN CONSTRUCTION GROUP, INC.

### 15. CONVERTIBLE DEBENTURES

	<u>2018</u> US\$	<u>2017</u> US\$
Balance, beginning of year	5,202,812	5,413,941
Interest charged	1,673,403	1,712,317
Interest paid	(367,184)	(780,606)
Redemption of convertible debentures	(1,139,125)	(1,155,446)
Conversion of convertible debentures	-	(1,390)
Effect of foreign currency exchange differences	(107,443)	13,996
Balance, end of year	<u>5,262,463</u>	<u>5,202,812</u>

Liability component of the convertible debentures is analyzed for reporting purpose as:

	<u>2018</u> US\$	<u>2017</u> US\$
Current liability	5,262,463	1,065,754
Non-current liability	-	4,137,058
	<u>5,262,463</u>	<u>5,202,812</u>

#### Convertible debentures - principal amount of CAD15,000,000

On November 1, 2010, the Company completed a prospectus offering of 15,000 unsecured subordinated convertible debentures at a price of CAD1,000 (equivalent to US\$987) per debenture for gross proceeds of CAD15,000,000 (equivalent to US\$14,799,000). Each convertible debenture bore interest at a rate of 10% per annum to be paid semi-annually in arrears and was due on October 31, 2015. Each convertible debenture, at the election of the holder, is convertible to 384.6153 common shares of the Company at a conversion price (subject to adjustment for among other things, subdivision or consolidation of shares, distribution of shares by way of dividend, cash dividend and options, rights or warrants) of CAD2.60 per share. The convertible debentures are redeemable by the Company at any time on or after November 1, 2013 at a price equal to the principal amount thereof plus accrued and unpaid interest if the common shares of the Company trade at a volume weighted average price not less than 125% of the conversion price of the debentures for the 20 most recent trading days with at least 1,000 shares traded in each trading day ending five trading days before the applicable redemption notice. The Company paid 6% agent's fee of CAD900,016 (equivalent to US\$887,940) agent's legal and related expenses of CAD410,149 (equivalent to US\$404,646) and other issue costs of CAD95,736 (equivalent to US\$94,451), totaling CAD1,405,901 (equivalent to US\$1,387,037).

The Company uses the residual value method to allocate the fair value of the convertible debentures between the liability and equity components. Under this method, the value of the equity component of CAD2,694,000 (equivalent to US\$2,657,900) was determined by deducting the fair value of the liability component from the fair value of the entire convertible debentures. The fair value of the liability component of CAD11,153,000 (equivalent to US\$11,003,593) was computed as the present value of future principal and interest payments discounted at a rate of 18% per annum. Debenture issue costs of CAD252,924 (equivalent to US\$249,530) were allocated to the equity component.

15. CONVERTIBLE DEBENTURES - continued

Convertible debentures - principal amount of CAD15,000,000 - continued

The principal amount of original convertible debentures outstanding as at June 30, 2014 was CAD15,000,000 (equivalent to US\$14,050,000).

On March 20, 2015, the debenture holders approved a modification to the terms of the convertible debentures. The following modifications have been made and are effective July 1, 2015:

- (i) The interest rate was increased from 10% to 11.5% per annum;
- (ii) A retraction right was added whereby CAD5,000,000 is redeemable by the Company, at the holder's option, on October 31, 2015 and CAD1,500,000 is redeemable by the Company, at the holder's option, on each of October 31, 2016 and October 31, 2017. The redemption price is equivalent to 100% of the principal amount thereof to be retracted, together with accrued and unpaid interest on the principal amount of the debentures;
- (iii) The maturity date was extended from October 31, 2015 to October 31, 2018;
- (iv) The conversion price was reduced from CAD2.60 per share to CAD1.00 per share; and
- (v) The restricted redemption period was extended to October 31, 2016.
- (vi) Prior to October 31, 2016, the convertible debentures are redeemable at the issuer's option at principal amount plus accrued and unpaid interest on not less than 30 days and not more than 60 days' notice in case the current market price of the Company's shares on the date on which the notice of redemption is given is not less than 125% of the conversion price. On and after October 31, 2016, the convertible debentures are redeemable at the issuer's option not less than 30 days and not more than 60 days' prior notice at principal amount plus accrued and unpaid interest.

The modification was considered an extinguishment of the existing convertible debenture and the recognition of a new convertible debenture as the modified terms were substantially different from the original terms. The carrying amount of liability and equity components of the existing convertible debentures on the date of approval of modification is CAD14,739,265 (equivalent to US\$11,702,473) and CAD2,087,236 (equivalent to US\$2,059,230), respectively. The Group engaged an independent valuer to carry out a fair value assessment on the liability component of the existing convertible debentures on that date, which is CAD13,711,246 (equivalent to US\$10,886,261) at a discount rate of 27.4%. As a result, a gain on extinguishment of the liability component of CAD1,028,019 (equivalent to US\$816,212), being the difference between the fair value and carrying amount of the liability component together with any closely related embedded derivatives on extinguishment date, is recognized in the statement of profit or loss. Furthermore, the Company incurred transaction costs of CAD717,807 (equivalent to US\$622,394) in relation to the modification, and recorded this against the gain on extinguishment of liability component, resulting in a net gain on extinguishment of CAD310,212 (equivalent to US\$193,818) recognized in the statement of profit or loss.

15. CONVERTIBLE DEBENTURES - continued

Convertible debentures - principal amount of CAD15,000,000 - continued

The fair value of the liability component, as well as the early redemption embedded derivatives of the modified convertible debentures on the date of modification are as follow:

- (i) Liability component was initially measured at fair value amounted to CAD10,070,966 (equivalent to US\$7,996,003), which represented the present value of the contractually determined stream of future cash flows discounted at the prevailing market interest rate at that time applicable to instruments of comparable credit status and providing substantially the same cash flows, on the same terms, but without the derivative components of 27.43% per annum;
- (ii) In the opinion of the management of the Company, the economic characteristics and risks of the early redemption options are closely related to the host debt contract of the convertible bonds. Therefore, the Company did not account for the early redemption options separately. The fair value of holders' and issuer's early redemption options amounting to CAD1,031,820 (equivalent to US\$819,230) was determined using a Binomial Option Pricing Model. The variables and assumptions used in computing the fair value are based on the management' best estimate. The value varies with different variables of certain subjective assumptions.

Inputs into the binomial model used to determine the fair value of the early redemption options on modification date:

Share price	CAD0.62
Exercise price	CAD1
Option life	3.62
Volatility	93%
Risk-free interest rate	0.51%
Dividend yield	0%

- (iii) The Company used the residual value method to allocate the fair value of the convertible debentures between the liability and equity components. Under this method, the value of equity component of CAD5,798,071 (equivalent to US\$4,603,470), was determined by deducting the fair value of liability component (included the closely related embedded derivatives) from the fair value of the entire convertible debentures.

On October 31, 2016 and 2015, the Company successfully retracted and redeemed CAD1,500,000 (equivalent to US\$1,155,446) and CAD5,000,000 (equivalent to US\$3,859,216) of its unsecured convertible debentures with the maturity date on October 31, 2018, respectively.

On January 3, 2017, 3 unsecured subordinated convertible debentures amount to CAD3,000 (equivalent to US\$2,311) were converted into 3,000 common shares with the conversion price of CAD1.00 per share, in which the relevant amount had been released from convertible debentures equity reserve and liability of convertible debentures.

On October 31, 2017, the Company successfully retracted and redeemed CAD1,500,000 (equivalent to US\$1,139,125) of its unsecured convertible debentures with the maturity date on October 31, 2018.



BOYUAN CONSTRUCTION GROUP, INC.

16. INCOME TAXES

Income tax expenses are as follows:

	<u>2018</u> US\$	<u>2017</u> US\$
Current tax:		
PRC Enterprise Income Tax ("PRC EIT")	5,311,447	4,384,836
Deferred tax:		
Current year	<u>(2,491,015)</u>	<u>(1,534,850)</u>
	<u>2,820,432</u>	<u>2,849,986</u>

Under the Law of the People's Republic of China on Enterprise Income Tax (the "EIT Law") and Implementation Regulation of the EIT Law, the tax rate of the PRC subsidiaries is 25% for both years.

Taxation arising in other jurisdictions is calculated at the rates prevailing in the relevant jurisdictions.

The Company is incorporated in Canada, which is the country in which the Company is domiciled, and is governed by the Income Tax Act of Canada. It is not anticipated to incur income taxes as no income is to be generated in Canada.

The income tax expense for the year can be reconciled to the profit before income taxes per the consolidated statements of profit or loss and other comprehensive income as follows:

	<u>2018</u> US\$	<u>2017</u> US\$
Profit before income taxes	<u>11,541,232</u>	<u>7,478,008</u>
Tax calculated at PRC EIT rate of 25% (June 30, 2017: 25%)	2,885,308	1,869,502
Increase (decrease) in income taxes resulting from:		
Tax effect of expenses not deductible for tax purpose	71,160	270,972
Tax effect of income not taxable for tax purpose	(1,504,772)	(1,546,791)
Tax effect of tax losses not recognized	<u>1,368,736</u>	<u>2,256,303</u>
	<u>2,820,432</u>	<u>2,849,986</u>

BOYUAN CONSTRUCTION GROUP, INC.

## 16. INCOME TAXES - continued

For the purpose of presentation in the consolidated statements of financial position, certain deferred tax assets and liabilities have been offset. The following is an analysis of the deferred tax balances for financial reporting purposes:

	Impairment losses on accounts receivable and unbilled <u>revenue</u> US\$	Timing differences on unbilled <u>revenue</u> US\$	Accelerated tax depreciation on plant and <u>equipment</u> US\$	<u>Total</u> US\$
At July 1, 2016	4,488,457	(2,681,557)	1,600,223	3,407,123
(Charged) credited to profit or loss	(59,239)	1,604,980	(10,891)	1,534,850
Effect of foreign currency exchange differences	88,419	(52,824)	31,523	67,118
At June 30, 2017	4,517,637	(1,129,401)	1,620,855	5,009,091
Credited (charged) to profit or loss	1,874,761	787,768	(171,514)	2,491,015
Effect of foreign currency exchange differences	(106,740)	26,685	(38,297)	(118,352)
At June 30, 2018	<u>6,285,658</u>	<u>(314,948)</u>	<u>1,411,044</u>	<u>7,381,754</u>

Under the EIT Law of the PRC, withholding tax is imposed on dividends declared in respect of profits earned by the PRC subsidiaries from January 1, 2008 onwards. Deferred taxation has not been provided for in the consolidated financial statements in respect of temporary differences attributable to the profits earned by the PRC subsidiaries amounting to approximately US\$137,478,000 (June 30, 2017: US\$117,216,000) as the Group is able to control the timing of the reversal of the temporary differences and it is probable that the temporary differences will not reverse in the foreseeable future.

As at June 30, 2018, the Group has unused tax losses of approximately US\$54,484,000 (June 30, 2017: US\$49,009,000) available for offset against future profits, which will expire from 2031 to 2036. No deferred tax asset has been recognized in respect of the tax losses due to the unpredictability of future profit streams.

BOYUAN CONSTRUCTION GROUP, INC.

17. GENERAL AND ADMINISTRATIVE EXPENSES

	<u>2018</u> US\$	<u>2017</u> US\$
General and administrative expenses comprise the following:		
Depreciation and amortization	591,837	692,551
Rental expenses	665,768	657,425
Office expenses	1,781,718	1,639,839
Salaries and other benefits	2,315,077	2,063,898
Others	761,807	1,446,654
Total	<u>6,116,207</u>	<u>6,500,367</u>

18. SHARE CAPITAL

(a) **Authorized**

Unlimited number of common shares without par value.

Unlimited number of Class A Series 1 preferred shares without par value, each preferred share is convertible to one common share at no additional consideration.

(b) **Issued common shares**

	<u>Number</u> <u>of shares</u>	<u>Amount</u> US\$
Balance at July 1, 2016	25,420,065	7,156,864
Conversion of convertible debentures (Note)	3,000	2,311
Balance at June 30, 2017, July 1, 2017 and June 30, 2018	<u>25,423,065</u>	<u>7,159,175</u>

Note: On January 3, 2017, 3 unsecured subordinated convertible debentures amount to CAD3,000 (equivalent to US\$2,311) were converted into 3,000 common shares with the conversion price of CAD1.00 per share, in which the relevant amount had been released from convertible debentures equity reserve and liability of convertible debentures (note 15).

18. SHARE CAPITAL - continued

(b) Issued common shares - continued

**Stock options**

The Company grants incentive stock options as permitted pursuant to the Company's Stock Option Plan (the "Plan") approved by the shareholders which complies with the rules and policies of the TSX. Under the Plan, the aggregate number of common shares which may be subject to option at any one time may not exceed 10% of the issued common shares of the Company as of that date including options granted prior to the adoption of the Plan. Options granted may not exceed a term of 5 years, and the term will be reduced to one year following the date of death of the optionee. If the optionee ceases to be qualified to receive options from the Company those options shall immediately expire. All options vest when granted unless otherwise specified by the Board of Directors.

As at June 30, 2018, the Company has stock options outstanding to directors and officers to acquire an aggregate of 1,755,000 (June 30, 2017: 1,755,000) common shares summarized as follows.

	<u>Underlying shares</u>	<u>Weighted average exercised price CAD</u>
Stock options outstanding at July 1, 2016, June 30, 2017, July 1, 2017 and June 30, 2018	<u>1,755,000</u>	<u>0.61</u>

Details of stock options outstanding:

<u>Expiry date</u>	<u>Exercise price</u>	<u>Stock options outstanding</u>		<u>Stock options exercisable and vested</u>	
		<u>2018</u>	<u>2017</u>	<u>2018</u>	<u>2017</u>
June 30, 2019	CAD0.61	1,755,000	1,755,000	1,755,000	1,755,000

During the year ended June 30, 2014, there were 1,755,000 options granted by the Company. One-third of the options vest on the grant date, one-third on June 30, 2015 and the remaining one-third on June 30, 2016. The fair value of the share options is determined using the Black-Scholes option pricing model on the date of issue to be US\$0.48 per option. The variables and assumptions used in computing the fair value of the share options are based on the managements' best estimate. The value of an option varies with different variables of certain subjective assumptions.

18. SHARE CAPITAL - continued

(b) Issued common shares - continued

**Stock options** - continued

The Company uses the Black-Scholes option pricing model to value stock options which requires management to make estimates that are subjective and may not be representative of actual results. Changes in assumptions can materially affect estimates of fair values. The key assumptions adopted in the valuation was as follows:

	<u>2014</u>
Share price at grant date	US\$0.62
Risk-free interest rate	1.53%
Expected dividend yield	0%
Expected option life	5 years
Expected stock price volatility	119%
Estimated forfeiture rate	0%

For the years ended June 30, 2018 and 2017, no share-based compensation expense related to the above options was charged to the statement of profit or loss.

19. RESERVES

Statutory reserve

Pursuant to PRC regulations, the Group is required to make appropriations to reserve funds, based on after tax net income determined in accordance with PRC generally accepted accounting principles. The reserve funds are established for covering corporate obligations in the event of business liquidation. The reserve funds are presented in the consolidated financial statements as statutory reserve but are not available for distribution to shareholders other than in liquidation and may limit repatriation of invested capital. The reserve funds accumulated by the Group as at June 30, 2018 was US\$14,437,387 (June 30, 2017: US\$12,323,657).

Contributed surplus

Contributed surplus comprises a) capital contribution from shareholders, b) share-based payment reserve, and c) the amount transferred from convertible debentures equity reserve attributable to the extinguished convertible debentures, net of the amount of consideration relating to the original equity component of convertible debentures upon their early extinguishment.

BOYUAN CONSTRUCTION GROUP, INC.

20. EARNINGS PER SHARE

The calculation of the basic and diluted earnings per share attributable to owners of the Company is based on the following data:

	<u>2018</u> US\$	<u>2017</u> US\$
<i>Earnings</i>		
Earnings for the purpose of basic earnings per share (represented by profit for the year)	8,720,800	4,628,022
Effect of diluted earnings per share:		
Interest on convertible debentures (net of income tax in Canada of 26%)	<u>1,238,318</u>	<u>1,267,115</u>
	<u>9,959,118</u>	<u>5,895,137</u>
	<u>2018</u>	<u>2017</u>
<i>Number of shares</i>		
Weighted average number of common shares for the purpose of basic earnings per share	25,423,065	25,421,536
Effect of dilutive potential common shares:		
Convertible debentures	<u>7,500,367</u>	<u>8,999,899</u>
Weighted average number of common shares for the purpose of diluted earnings per share	<u>32,923,432</u>	<u>34,421,435</u>
	<u>2018</u> US\$	<u>2017</u> US\$
Basic earnings per common share	<u>0.34</u>	<u>0.18</u>
Diluted earnings per common share	<u>0.30</u>	<u>0.17</u>

For the years ended June 30, 2018 and 2017, the computation of diluted earnings per share does not assume the exercise of the Company's outstanding share options because the exercise price of those options was higher than the average market price.

## BOYUAN CONSTRUCTION GROUP, INC.

### 21. EMPLOYEE BENEFITS/COSTS OF CONSTRUCTION

The employees of the Group's subsidiaries are members of a state-managed retirement benefits scheme operated by the PRC government. The subsidiaries are required to contribute a certain percentage of payroll cost to the retirement benefits scheme to fund the benefits. The only obligation of the Group with respect to the retirement benefits scheme is to make the specified contributions.

For the years ended June 30, 2018 and 2017, the Group incurred the following employee compensation expenses:

	<u>2018</u> US\$	<u>2017</u> US\$
Salaries, bonus and other short-term employee benefits	3,835,850	2,546,321
Contributions to retirement benefit scheme	579,380	426,813
	<u>4,415,230</u>	<u>2,973,134</u>

Staff costs of US\$2,315,077 (June 30, 2017: US\$2,063,898) and US\$2,100,153 (June 30, 2017: US\$909,236) were charged to general and administrative expenses and costs of construction, respectively.

Staff costs of US\$55,926,835 (June 30, 2017: US\$21,886,648) related to construction site workers who are employed by personnel service company of the Group, are excluded from the amounts above and are included in the costs of construction.

Cost of materials of US\$168,168,038 and sub-contracting cost of US\$46,306,970 (June 30, 2017: US\$148,328,425 and US\$8,546,714) incurred in the construction works, are included in the costs of construction.

### 22. SEGMENTED INFORMATION

Management has determined the operating segments based on the reports reviewed by the Managing Director of the Company, being the chief operating decision maker, that are used to make strategic decisions. The Group has one operating segment, being the construction of residential and business buildings, municipal infrastructure and engineering projects in PRC. All of the Group's revenue was generated in the PRC and substantially all capital assets are located in the PRC.

## BOYUAN CONSTRUCTION GROUP, INC.

### 23. OTHER FINANCIAL LIABILITIES/CONTINGENT LIABILITIES

As at June 30, 2018 and 2017, the Group has guaranteed the bank loans for other construction companies, in amounts totaling US\$21,901,752 (June 30, 2017: US\$30,574,451). No consideration has been specifically received by the Group for these guarantees and are designated as at fair value through profit or loss.

During the years ended June 30, 2018 and 2017, the Group engaged an independent qualified professional valuer to assess the fair value of the financial guarantee contracts at initial recognition. The fair value of financial guarantee contracts upon recognition is determined using option pricing models where the main assumptions are the probability of default by the specified counterparty extrapolated from market-based credit information and the amount of expected loss, as a result of the default.

The carrying amount of the Group's financial guarantee contracts amounted to US\$350,460 (June 30, 2017: US\$1,736,706) represented the amount of obligation under these contracts as at June 30, 2018. As a result, a fair value gain of US\$1,386,246 (June 30, 2017: a fair value loss of US\$496,635) was recognized in the statement of profit or loss for the year ended June 30, 2018.

### 24. OTHER INCOME

Other income comprises the following:

	<u>2018</u> US\$	<u>2017</u> US\$
Imputed interest on accounts receivable and unbilled revenue	4,632,842	5,823,959
Bank interest income	157,481	170,375
	<u>4,790,323</u>	<u>5,994,334</u>

### 25. INTEREST EXPENSE

	<u>2018</u> US\$	<u>2017</u> US\$
Interest on bank loans wholly repayable within a year	3,514,061	4,072,697
Interest on convertible debentures	1,673,403	1,712,317
Interest on bank notes payable	474,553	265,894
Interest on discounted bank notes	1,135,093	-
	<u>6,797,110</u>	<u>6,050,908</u>



## BOYUAN CONSTRUCTION GROUP, INC.

### 26. DIVIDEND

During the years ended June 30, 2018 and 2017, no dividends were declared or paid to the shareholders.

No final dividend has been proposed in respect of the years ended June 30, 2018 and 2017.

### 27. OPERATING LEASES

#### **The Group as lessee**

	<u>2018</u> US\$	<u>2017</u> US\$
Minimum lease payments paid under operating leases during the year	<u>665,768</u>	<u>657,425</u>

At the end of the reporting period, the Group had commitments for future minimum lease payments under non-cancellable operating leases which fall due as follows:

	<u>2018</u> US\$	<u>2017</u> US\$
Within one year	709,600	697,830
In the second to fifth years inclusive	<u>1,364,596</u>	<u>2,018,976</u>
	<u>2,074,196</u>	<u>2,716,806</u>

Operating lease payments represent rentals payable for office premise in Zhejiang and Hainan, the PRC. Leases are negotiated for terms ranging from one to five years.

#### **The Group as lessor**

The Group leased part of its building under operating lease arrangements. Leases are negotiated for terms of 1 to 2 years.

At the end of the reporting period, the Group had contracted with tenants for the following future minimum lease payments which fall due as follows:

	<u>2018</u> US\$	<u>2017</u> US\$
Within one year	44,792	25,193
In the second to fifth years inclusive	<u>8,402</u>	<u>-</u>
	<u>53,194</u>	<u>25,193</u>

28. CAPITAL MANAGEMENT

The Group's objectives when managing capital are:

- to safeguard the Group's ability to continue as a going concern, so that it can continue to provide returns for shareholders and benefits for other stakeholders, and
- to provide an adequate return to shareholders through expansion correspondingly to the level of risk.

Management of the Company defines capital as shareholders' equity, borrowings, bank notes payable, other loans and convertible debentures.

The Group is required to maintain a certain level of deposits with its banks as compensating balances for borrowings provided by these banks. The Group is not subject to any other externally imposed capital requirements.

The Group sets the amount of capital in proportion to risk. The Group manages the capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of the underlying assets. In order to maintain or adjust the capital structure, the Group may issue new shares, sell assets, reduce debt or increase its debt.

29. FINANCIAL INSTRUMENTS

	<u>2018</u> US\$	<u>2017</u> US\$
<b>Financial assets</b>		
Loans and receivables		
Unbilled revenue	139,783,087	116,433,106
Accounts receivable	70,311,783	63,914,686
Bank notes receivables	9,750,832	-
Deposits	13,707,647	10,300,761
Other receivables	1,555,738	1,146,929
Due from related parties	811,674	55,139
Restricted cash	8,546,215	6,825,097
Cash and cash equivalents	7,236,990	3,996,016
	<u>251,703,966</u>	<u>202,671,734</u>
<b>Financial liabilities</b>		
At amortized cost		
Borrowings	75,299,783	66,776,845
Accounts and other payables	11,341,264	7,840,422
Bank notes payable	24,421,208	10,882,557
Other loans	643,698	3,778,113
Convertible debentures	5,262,463	5,202,812
Financial guarantee contracts	350,460	1,736,706
	<u>117,318,876</u>	<u>96,217,455</u>

The Group's financial instruments are exposed to certain financial risks including market risk (currency risk and interest rate risk), credit risk and liquidity risk.

29. FINANCIAL INSTRUMENTS - continued

**Market risk**

*Foreign currency risk*

The Group has limited foreign currency exposure as the amounts of foreign currency monetary assets and liabilities held by the Group at the end of the reporting date are minimal. The management conducts periodic review of the exposure and requirements of various currencies, and will consider hedging significant foreign currency exposures should the need arise.

*Interest rate risk*

The Group is exposed to fair value interest rate risk in relation to fixed-rate borrowings (note 12). The Group is also exposed to cash flow interest rate risk in relation to variable-rate restricted cash, cash and cash equivalents and borrowings (note 12).

The Group does not currently hold any financial instruments that mitigate these risks. Unfavourable changes in the applicable interest rate may result in an increase in interest expense.

The Group's cash flow interest rate risk is mainly concentrated on the fluctuation of prime rate in PRC arising from the Group's borrowings disclosed in note 12 to the consolidated financial statements.

*Sensitivity Analysis*

The sensitivity analysis has been determined based on the exposure to interest rate risk for variable-rate restricted cash, cash and cash equivalents and borrowings. The analysis is prepared assuming the financial instruments outstanding at the end of the reporting period were outstanding for the whole year and all other variables were held constant.

*Bank balances*

If interest rates had been 100 basis points (June 30, 2017: 100 basis points) higher/lower and all other variables were held constant, the Group's post-tax profit for the year would increase/decrease by approximately US\$118,000 (June 30, 2017: US\$81,000). This is mainly attributable to the Group's exposure to interest rates on its variable-rate bank balances.

*Borrowings*

If interest rates had been 100 basis points (June 30, 2017: 100 basis points) higher/lower and all other variables were held constant, the Group's post-tax profit for the year would decrease/increase by approximately US\$373,000 (June 30, 2017: US\$246,000). This is mainly attributable to the Group's exposure to the interest rates on its variable-rate borrowings.

29. FINANCIAL INSTRUMENTS - continued

**Credit risk**

As at June 30, 2018, other than those financial assets whose carrying amounts best represent the maximum exposure to credit risk, the Group's maximum exposure to credit risk which will cause a financial loss to the Group arising from the amount of contingent liabilities in relation to financial guarantees provided by the Group is disclosed in note 23.

Credit risk from accounts receivable, unbilled revenue and deposits to customers encompasses the default risk of customers and non-performance by customers in accordance with contractual terms. The Group's customers are for the most part, private companies located in the PRC. Its exposure to credit risk with its customers is influenced mainly by the individual characteristics of each customer. The Group's exposure to credit risk associated with its accounts receivable, unbilled revenue and deposits to customers is the risk that a customer will be unable to pay amounts due to the Group. In its determination of valuation of accounts receivable, unbilled revenue and deposits to customers, including the allowance for doubtful accounts, management relies on current customer information and its planned course of action as well as assumptions about business and economic conditions in the future period over which the receivables are collectible. Allowances are provided for potential losses that have been incurred at the end of the reporting period. The amounts disclosed on the statements of financial position are net of these allowances for doubtful debts. Accounts receivables, unbilled revenue and deposits to customers are considered for impairment on a case-by-case basis when they are past due or when objective evidence is received that a customer will default.

Management takes into consideration the customer's payment history, the credit worthiness and the current economic environment in which the customer operates to assess impairment. Management, on an ongoing basis, monitor the level of accounts receivable, unbilled revenue and deposits to customers attributable to each customer and the length of time taken for amounts to be settled and where necessary, takes appropriate action to follow up on those balances considered overdue.

Under PRC regulations, a general contractor is entitled to first claim against assets of its customers subject to certain conditions, which gives a general contractor a "mechanic lien" senior to all other secured debt including bank borrowings, bank notes and any payables. If a customer defaults on the payment on the contract with the Group, the customer can be liable to surrender the real estate property and the land use rights associated with the real estate property that is under construction.

In this regard, the management of the Company consider that the Group's credit risk in relation to the accounts receivable, unbilled revenue and deposits to customers are significantly reduced.

As of June 30, 2018, revenue from the top three customers accounted for 22% (June 30, 2017: 20%) of total revenue. The outstanding amounts owed by top three accounts receivable and unbilled revenue accounted for 42% and 25% (June 30, 2017: 34% and 37%) of the total accounts receivable and unbilled revenue, respectively.

29. FINANCIAL INSTRUMENTS - continued

**Credit risk** - continued

The management of the Company consider that the Group has adequate credit control for determination of credit limits, credit approvals and other monitoring procedures to ensure that follow-up actions are taken to recover overdue debts. In addition, the Group reviews the recoverable amount of each individual trade debt and unbilled revenue accounts at the end of each reporting period to ensure that adequate impairment losses are made against the irrecoverable amounts.

Based on management's assessment, there are no changes in the credit quality of the remaining customers. They are customers with long trading history with the Group and no default payment, the credit risk from these customers is mitigated.

The Group's bank balances and restricted cash are held in large PRC and Hong Kong banks. These assets have low credit risk due to the financial strength and credibility of the banks.

The Group had concentration of credit risk by geographical locations as all the accounts receivable and unbilled revenue are located in the PRC as at June 30, 2018 and 2017.

**Liquidity risk**

Liquidity risk is the risk that the Group is not able to meet its financial obligations as they fall due. The Group's approach to managing liquidity risk is to ensure that sufficient cash and credit facilities are available to meet liabilities when due. The contractual maturities of the Group's other loans and convertible debentures are described in notes 14 and 15, respectively. The remaining financial liabilities, consisting of borrowings, bank notes payable and accounts payable, are expected to be realized within one year. Their carrying value on the consolidated statements of financial position are stated as undiscounted cash flow based on the earliest date on which the Group can be required to satisfy the liabilities.

The table represents undiscounted cash flow for current and non-current portion of financial liabilities as at June 30, 2018 and 2017. The undiscounted cash flow includes both interest and principal cash flows. For other financial liabilities, all balances are due within 1 year and the undiscounted cash flows are approximated to the carrying amount. To the extent that interest flows are floating rate, the undiscounted amount is derived from interest rate at the end of the reporting period:

	Weighted average <u>interest rate</u> %	Less than <u>1 year</u> US\$	1 - 2 <u>years</u> US\$	2 - 5 <u>years</u> US\$	Total undiscounted <u>cash flows</u> US\$	Carrying <u>amount</u> US\$
<b>At June 30, 2018</b>						
Borrowings	5.8	76,174,290	-	-	76,174,290	75,299,783
Accounts and other payables	-	11,341,264	-	-	11,341,264	11,341,264
Bank notes payable	1.9	24,586,329	-	-	24,586,329	24,421,208
Other loans	-	643,698	-	-	643,698	643,698
Convertible debentures	33.8	5,521,927	-	-	5,521,927	5,262,463
Financial guarantee contracts (Note)	-	21,901,752	-	-	21,901,752	350,460
		<u>140,169,260</u>	<u>-</u>	<u>-</u>	<u>140,169,260</u>	<u>117,318,876</u>

29. FINANCIAL INSTRUMENTS - continued

**Liquidity risk - continued**

	Weighted average <u>interest rate</u> %	Less than <u>1 year</u> US\$	1 - 2 <u>years</u> US\$	2 - 5 <u>years</u> US\$	Total undiscounted <u>cash flows</u> US\$	Carrying <u>amount</u> US\$
<b>At June 30, 2017</b>						
Borrowings	4.9	67,610,134	-	-	67,610,134	66,776,845
Accounts and other payables	-	7,840,422	-	-	7,840,422	7,840,422
Bank notes payable	2.0	10,988,159	-	-	10,988,159	10,882,557
Other loans	-	3,769,693	8,420	-	3,778,113	3,778,113
Convertible debentures	33.8	1,820,313	5,601,043	-	7,421,356	5,202,812
Financial guarantee contracts (Note)	-	30,574,451	-	-	30,574,451	1,736,706
		122,603,172	5,609,463	-	128,212,635	96,217,455

Note: The amounts included above for financial guarantee contracts are the maximum amounts the Group could be forced to settle under the arrangement for the full guaranteed amount if that amount is claimed by the counterparty to the guarantee. Based on expectations at the end of the reporting period, the Group considers that it is more likely than not that such an amount will not be payable under the arrangement. However, this estimate is subject to change depending on the probability of the counterparty claiming under the guarantee which is a function of the likelihood that the financial receivables held by the counterparty which are guaranteed suffer credit losses.

**Fair value**

- (i) Fair value of the Group's financial liabilities that are measured at fair value on a recurring basis

Financial guarantee contracts issued by the Group are measured at fair value at the issue date and at the end of each reporting period. The following table gives information about how the fair values of these financial guarantee contracts are determined (in particular, the valuation technique(s) and input used), as well as the level of the fair value hierarchy into which the fair value measurements are categorized (Level 1 to 3) based on the degree to which the inputs to the fair value measurements is observable.

<u>Financial liabilities</u>	<u>Fair value</u>	<u>Fair value hierarchy</u>	<u>Valuation technique and key inputs</u>	<u>Relationship of unobservable inputs to fair value</u>
Financial guarantees provided for other construction companies	Liabilities - US\$350,460 as at June 30, 2018 (June 30, 2017: US\$1,736,706)	Level 3	Credit rating analysis key unobservable inputs: default rate, recovery rate and probability of default	The higher the default rate, the higher the fair value.  The higher the recovery rate, the lower the fair value.  The higher the probability of default, the higher the fair value.

BOYUAN CONSTRUCTION GROUP, INC.

29. FINANCIAL INSTRUMENTS - continued

**Fair value** - continued

(ii) Reconciliation of Level 3 fair value measurements

June 30, 2018

	Financial guarantee contracts US\$
Opening balance	(1,736,706)
Total gain recognized in profit or loss	<u>1,386,246</u>
Closing balance	<u><u>(350,460)</u></u>

June 30, 2017

	Financial guarantee contracts US\$
Opening balance	(1,240,071)
Total loss recognized in profit or loss	<u>(496,635)</u>
Closing balance	<u><u>(1,736,706)</u></u>

The financial liabilities subsequently measured at fair value on Level 3 fair value measurement represents contingent liabilities relating to financial guarantee on bank loans for other construction companies.

(iii) Fair value of the Group's financial assets and financial liabilities that are not measured at fair value on a recurring basis.

The Group considers that the carrying amounts of other financial assets and financial liabilities recorded at amortized cost in the consolidated financial statements approximate their fair value, which is determined in accordance with generally accepted pricing models based on discounted cash flow analysis.

## BOYUAN CONSTRUCTION GROUP, INC.

### 30. RECONCILIATION OF LIABILITIES ARISING FROM FINANCING ACTIVITIES

The table below details changes in the Group's liabilities arising from financing activities, including both cash and non-cash changes. Liabilities arising from financing activities are those for which cash flows were, or future cash flows will be, classified in the Group's consolidated statements of cash flows as cash flows from financing activities.

	<u>Borrowings</u>	<u>Other</u>	<u>Bank notes</u>	<u>Convertible</u>	<u>Total</u>
	<u>US\$</u>	<u>loans</u>	<u>payable</u>	<u>debentures</u>	<u>US\$</u>
	(Note 12)	(Note 14)	(Note 11(a))	(Note 15)	
At July 1, 2017	66,776,845	3,778,113	10,882,557	5,202,812	86,640,327
Financing cash flows	3,388,443	(3,290,731)	13,037,845	(1,506,309)	11,629,248
Interest expense	3,514,061	-	474,553	1,673,403	5,662,017
Effect of foreign currency exchange differences	<u>1,620,434</u>	<u>156,316</u>	<u>26,253</u>	<u>(107,443)</u>	<u>1,695,560</u>
At June 30, 2018	<u>75,299,783</u>	<u>643,698</u>	<u>24,421,208</u>	<u>5,262,463</u>	<u>105,627,152</u>

### 31. PARTICULARS OF PRINCIPAL SUBSIDIARIES OF THE COMPANY

The Group's significant subsidiaries as at the end of the year are as follows:

<u>Name</u>	Place of incorporation/ <u>operations</u>	<u>Attributable equity</u> <u>interest of the Group</u>				<u>Principal activities</u>
		<u>Directly</u>		<u>Indirectly</u>		
		<u>2018</u>	<u>2017</u>	<u>2018</u>	<u>2017</u>	
		%	%	%	%	
Hong Kong Wealthy Holdings Ltd.	Hong Kong	100	100	-	-	Investment holding
China Privco	The PRC	-	-	100	100	Purchasing arm of construction raw materials
Zhejiang Boyuan*	The PRC	-	-	-	-	Construction of residential and commercial buildings, municipal infrastructure and engineering projects

\* The Company has control over Zhejiang Boyuan through Contractual Arrangement.



## **BOYUAN CONSTRUCTION GROUP, INC.**

### **Management's Discussion and Analysis**

**September 28, 2018**

This Management's Discussion and Analysis (“**MD&A**”) relates to the financial condition and results of operations of Boyuan Construction Group, Inc. (the “**Company**”) for the fiscal year ended June 30, 2018 (“**FY2018**”) and the fiscal year ended June 30, 2017 (“**FY2017**”). It should be read in conjunction with the audited consolidated financial statements for FY2018 and FY2017 and notes thereto. The United States dollars is the Company's reporting currency and all figures herein are in United States dollars unless otherwise indicated. Boyuan reported its financial results in accordance with International Financial Reporting Standards (**IFRS**), as required for public companies in Canada. Additional information about Boyuan including the Company's Annual Information Form and other filings are available through the System for Electronic Document Analysis and Retrieval (**SEDAR**) at [www.sedar.com](http://www.sedar.com).

#### **Caution Regarding Forward-Looking Information:**

Certain information contained in this MD&A constitutes forward-looking information, which is information relating to future events or the Company's future performance and which is inherently uncertain. All information other than statements of historical fact may be forward-looking information. Forward-looking information is often, but not always, identified by the use of words such as “seek”, “anticipate”, “budget”, “plan”, “continue”, “estimate”, “expect”, “forecast”, “may”, “will”, “project”, “predict”, “potential”, “targeting”, “intend”, “could”, “might”, “should”, “believe” and similar words or phrases (including negative variations) suggesting future outcomes or statements regarding an outlook. Forward-looking information contained in this MD&A includes, but is not limited to, management’s belief in the level of credit risk arising from the Company’s customers, management’s expectation on the effectiveness of the Company’s disclosure controls and internal controls, management’s plan to implement independent consultant’s recommendations on internal controls and the plan to engage the consultant to perform an updated review on the internal control system, the Company's outlook on China's ongoing expansion of middle class and the growth of China's tier-2 cities and on the continued demand for the Company's services, the Company's plan to increase focus on specialty construction projects, the Company's expectation of higher profit margins for the specialty construction projects, and the Company's plan to upgrade its construction licences and qualifications. Forward-looking information involves known and unknown risks, uncertainties and other factors that may cause actual results or events to differ materially from those anticipated in such forward-looking information. The Company believes the expectations reflected in the forward-looking information are reasonable but no assurance can be given that these expectations will prove to be correct and readers are cautioned not to place undue reliance on forward-looking information contained in this MD&A. Some of the risks and other factors which could cause results to differ materially from those expressed in the forward-looking information contained in this MD&A include, but are not limited to: risk of the current depressed property market in China, risk of macro-economy cycle, risk from competition, risk from insufficient marketing to secure new projects, risk in obtaining additional financing, risk involving permits and licenses, reliance on key management member, risk from supply of raw materials, risk of financial leverage, risk of bad debts in accounts receivables, risk involved in real estate

development, foreign exchange fluctuations, political and economic conditions in China and other risks included in the Company's Annual Information Form for FY2018 and in the Company's other public disclosure documents filed with certain Canadian securities regulatory authorities and available at [www.sedar.com](http://www.sedar.com). The forward-looking information contained in this MD&A are made as of the date hereof and the Company undertakes no obligation to update publicly or revise any forward-looking information, whether as a result of new information, future events or otherwise, except as otherwise required by law.

## **OVERVIEW OF BUSINESS**

### ***About Boyuan***

Based in Jiaxing City, China, Boyuan Construction Group, Inc. is in the business of residential and commercial building construction, municipal infrastructure and engineering projects. The Company operates as a general contractor across China. Having a national class I construction qualification, the Company is qualified to participate in construction projects up to 40 storeys with a gross construction area of 200,000 square meters and with a contract value of less than five times of the registered capital of Zhejiang Boyuan Construction Co., Ltd., the operating entity in China.

The Company has completed 32 material projects in the past three fiscal years. Currently the Company has a significant project backlog including residential, commercial, industrial, and hotels. The duration of these projects ranges from one to three years. The majority of these projects are located in the Yangtze River Delta and Hainan Island.

The Company's common shares are publicly traded on the Toronto Stock Exchange (the "**Exchange**" or the "**TSX**") under the symbol "**BOY**". The Company's 11.5% unsecured convertible debentures due on October 31, 2018 (the "**Unsecured Debentures**") are traded on the Exchange under the symbol "**BOY.DB.A**".

## **OVERALL PERFORMANCE**

Revenue for FY2018 was \$325.9 million, up from \$199.5 million for FY2017. Net income after taxes for FY2018 was \$8.7 million or \$0.34 basic earnings per share and \$0.30 diluted earnings per share. This compares to \$4.6 million, or \$0.18 basic earnings per share and \$0.17 diluted earnings per share, for FY2017.

## **SELECTED ANNUAL FINANCIAL INFORMATION**

The following selected consolidated financial information has been derived from the Company's audited consolidated financial statements for the three years ended June 30, 2018, 2017 and 2016:

US\$'000 (except earnings per share amounts)	2018	2017	2016
Operating Results			
Construction revenue	325,926	199,514	200,954
Costs of construction	301,525	182,490	182,637
Gross profit	24,401	17,024	18,317
Net income	8,721	4,628	5,238
Earnings per share			
Basic	0.34	0.18	0.21
Diluted	0.30	0.17	0.20
Financial Position			
Current assets	210,336	157,611	176,243
Non-current assets	62,281	59,040	69,091
Total assets	272,617	216,651	245,334
Current liabilities	157,022	108,124	138,722
Long term debt	-	4,146	4,357
Shareholders' equity	115,595	104,381	102,255
Cash dividend per share	Nil	Nil	Nil
Common shares outstanding	25,423,065	25,423,065	25,420,065

## RESULTS OF OPERATIONS

Revenue for FY2018 was \$325.9 million, up 63.4% from \$199.5 million for FY2017. Revenue is recognized on the percentage-of-completion method. Revenue generated by new projects this year was able to offset the reduction in revenue from completed projects during the year. The measures introduced by the Chinese central government a few years ago to cool down the real estate market have had a negative impact on our business activities resulting in slower growth in revenue and a smaller gross margin in the past three years. The Company was also more selective in taking up new construction projects under the uncertain economic environment. This strategy has become the Company's main focus in the past few years in order to manage the Company's cash flows, as the protracted collection period of existing customers has had a negative impact on the cash flows. However, due to the relatively robust real estate market in Jiaxing, Zhejiang province in the past year, the Company was able to identify a number of high quality projects and as a result for the financial year ended June 30, 2018, the Company has commenced construction on thirteen material new projects with an aggregate contract value of \$315 million. Twelve of these thirteen projects are in the Jiaxing and its surrounding area. New projects taken up in FY2018, FY2017 and FY2016 amounted to \$315 million, \$260 million, and \$86 million, respectively. Most of the Company's projects have duration between 1 to 3 years.

The substantial increase in revenue this year was primarily due to the following new projects that commenced construction in the current year.

<b>Project</b>	<b>Revenue in FY2018(\$M)</b>
1. A residential project in Jiaxing, Zhejiang	18.0
2. A residential project in Jiaxing, Zhejiang	22.0
3. A manufacture facility in Jiaxing, Zhejiang	9.0
4. A residential project in Jiaxing, Zhejiang	15.8
5. A residential project in Haining, Zhejiang	11.0

Costs of construction for FY2018 were \$301.5 million, compared to \$182.5 million for FY2017. Costs of construction include all direct material, labour, subcontract and other related costs, such as equipment repairs. The two major components of the costs of construction are direct material and labour costs. Direct material costs were \$213.5 million and labour cost was \$75.9 million in FY2018. In comparison, direct material costs and labour costs were \$130.1 million and \$47.9 million in FY2017.

Gross profit for FY2018 was \$24.4 million, representing a margin of 7.5% on revenue. Gross profit for FY2017 was \$17.0 million, representing a margin of 8.5% on revenue. Due to the current real estate market environment in China, the Company has been experiencing a decreasing trend in gross margins in the past few years.

Other income was \$4.8 million in FY2018, compared to \$6.0 million in FY2017. Imputed interest on accounts receivable and unbilled revenue of \$4.6 million and \$5.8 million was recorded to other income for the years ended June 30, 2018 and 2017, respectively.

There was an impairment loss recovered on deposits of \$0.7 million in the year, compared to a loss of \$0.6 million last year. These amounts were included in the G&A expenses last year. G&A expenses were \$6.1 million in FY2018 compared to \$6.5 million in FY2017. The decrease was mainly due to the reclassification of the impairment loss/recovered on deposits during the years.

The net impairment loss on accounts receivable and unbilled revenue was \$6.8 million for FY2018 (\$1.9 million for FY2017). The impairment loss was a result of two projects in Hainan and a project in Haining that the Company has experienced a long delay in collection. On the other hand, the Company has recovered certain amount from accounts previously impaired thus resulting in a net impairment loss of \$6.8 million this year.

Interest expense was \$6.8 million in FY2018, an increase of \$0.7 million over FY2017. The higher interest expense for the year was primarily due to the increase in the bank notes payable in the year.

The gain on fair value change of financial guarantee contracts was \$1.4 million for FY2018 (loss of \$0.5 million for FY2017) was related to the carrying amount of the financial guarantee contracts, representing the amount of obligation under these contracts as at June 30, 2018. The fair value of the financial guarantee contracts was assessed by an independent qualified professional valuator. The fair value of financial guarantee contracts upon recognition is determined using option pricing models where the main assumptions are the probability of default by the specified counterparty extrapolated from market-based credit information and the amount of expected loss, as a result of the default. The carrying amount of financial guarantee contracts amounted to \$0.4 million at June

30, 2018 as compared to \$1.7 million as at June 30, 2017. The decrease has resulted in the gain on fair value change of financial guarantee contracts this year.

After-tax net income for FY2018 was \$8.7 million or \$0.34 basic earnings per share and \$0.30 diluted earnings per share compared to \$4.6 million or \$0.18 basic earnings per share and \$0.17 diluted earnings per share, for FY2017. The increase was principally due to higher revenue recorded this year.

Boyuan had working capital of \$53.3 million, including cash, cash equivalents, and restricted cash totalling \$15.8 million as at June 30, 2018. This compares to \$49.5 million and \$10.8 million, respectively, at June 30, 2017.

#### **FOURTH QUARTER RESULTS**

The following table sets forth the selected financial information in the three months ended June 30, 2018 and 2017:

US\$'000 (except earnings per share amounts)	Three months ended June 30	Three months ended June 30
Operating Results	2018	2017
Revenue	83,845	46,958
Cost of construction	77,300	44,328
Gross profit	6,545	2,630
Net Income	3,218	326
Earnings per share		
Basic	0.13	0.01
Diluted	0.10	0.01

Revenue for the three-month period ended June 30, 2018 was \$83.8 million, up 78.3% from \$47.0 million for Q4 FY2017. Cost of construction for Q4 FY2018 was \$77.3 million, up 74.3% from \$44.3 million for Q4 FY2017. The increase in revenue was mainly due to the increased number of new construction projects over the past year.

Gross profit for Q4 FY2018 was \$6.5 million, representing a margin of 7.8% on revenue. Gross profit for Q4 FY2017 was \$2.6 million, representing a margin of 5.6% on revenue.

The net income for Q4, FY2018 was \$3.2 million, with basic and diluted earnings per share of \$0.13 and \$0.10 respectively. For the same period last year, the net income was \$0.3 million, with \$0.01 basic and diluted earnings per share.

#### **Significant Accounting Policies**

##### Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and entities (including a special purpose entity) controlled by the Company and its subsidiaries.

Control is achieved when the Company:

- has power over the investee;
- is exposed, or has rights, to variable returns from its involvement with the investee; and
- has the ability to use its power to affect its returns.

The Group reassesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control listed above.

Consolidation of a subsidiary begins when the Group obtains control over the subsidiary and ceases when the Group loses control of the subsidiary. Specifically, income and expenses of a subsidiary acquired or disposed of during the year are included in the consolidated statements of profit or loss and other comprehensive income from the date the Group gains control until the date when the Group ceases to control the subsidiary.

#### *Recognition of revenue*

Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for services provided in the normal course of business, net of discounts and sales related taxes.

Revenue is recognized when the amount of revenue can be reliably measured; when it is probable that future economic benefits will flow to the Group and when specific criteria have been met for each of the Group's activities, as described below.

Where the outcome of a construction contract can be estimated reliably, revenue and costs are recognized by reference to the stage of completion of the contract activity at the end of the reporting period, measured based on the proportion of contract costs incurred for work performed to date relative to the estimated total contract costs. Variations in contract work, claims and incentive payments are included to the extent that the amount can be measured reliably and its receipt is considered probable.

Where the outcome of a construction contract cannot be estimated reliably, contract revenue is recognized to the extent of contract costs incurred that it is probable will be recoverable. Contract costs are recognized as expenses in the period in which they are incurred.

When it is probable that total contract costs will exceed total contract revenue, the expected loss is recognized as an expense immediately in the statement of profit or loss.

Amounts billed for work performed but not yet paid by the customer are included in the consolidated statement of financial position under accounts receivable.

The Group presents as an asset as unbilled revenue the amount due from customers for contract work for all completed contracts and contracts in progress for which costs incurred plus recognized profits (less recognized losses) exceed progress billings. The Group presents as a liability as

deferred revenue the amount due to customers for contract work for contracts in progress for which progress billings exceed costs incurred plus recognized profits (less recognized losses).

## **Application of New and Revised IFRSs<sup>[1]</sup>**

### Amendments to IFRSs that are mandatorily effective for the current year

The Group has applied the following amendments to IFRSs issued by the International Accounting Standards Board ("IASB") for the first time in the current year:

Amendments to IAS 7      Disclosure Initiative<sup>[1]</sup>

Amendments to IAS 12      Recognition of Deferred Tax Assets for Unrealised Losses

Amendments to IFRS 12      <sup>[1]</sup>As part of the Annual Improvements to IFRSs 2014 - 2016 Cycle

### Amendments to IAS 7 Disclosure Initiative

The Group has applied these amendments for the first time in the current year. The amendments require an entity to provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both cash and non-cash changes. In addition, the amendments also require disclosures on changes in financial assets if cash flows from those financial assets were, or future cash flows will be, included in cash flows from financing activities.

Specifically, the amendments require the following to be disclosed: (i) changes from financing cash flows; (ii) changes arising from obtaining or losing control of subsidiaries or other businesses; (iii) the effect of changes in foreign exchange rates; (iv) changes in fair values; and (v) other changes.

A reconciliation between the opening and closing balances of these items is provided in note 30. Consistent with the transition provisions of the amendments, the Group has not disclosed comparative information for the prior year. Apart from the additional disclosure in note 30, the application of these amendments has had no impact on the Group's consolidated financial statements.

Except as described above, the application of the amendments to IFRSs in the current year has had no material impact on the Group's financial performance and positions for the current and prior years and/or on the disclosures set out in these consolidated financial statements.

New and revised IFRSs in issue but not yet effective

The Group has not early applied the following new and revised IFRSs that have been issued but are not yet effective:

IFRS 9	Financial Instruments <sup>1</sup>
IFRS 15	Revenue from Contracts with Customers and the related Amendments <sup>1, [1], [2], [3], [4], [5], [6], [7], [8], [9], [10], [11], [12], [13], [14], [15], [16], [17], [18], [19], [20], [21], [22], [23], [24], [25], [26], [27], [28], [29], [30], [31], [32], [33], [34], [35], [36], [37], [38], [39], [40], [41], [42], [43], [44], [45], [46], [47], [48], [49], [50], [51], [52], [53], [54], [55], [56], [57], [58], [59], [60], [61], [62], [63], [64], [65], [66], [67], [68], [69], [70], [71], [72], [73], [74], [75], [76], [77], [78], [79], [80], [81], [82], [83], [84], [85], [86], [87], [88], [89], [90], [91], [92], [93], [94], [95], [96], [97], [98], [99], [100]</sup>
IFRS 16	Leases <sup>2</sup>
IFRS 17	Insurance Contracts <sup>4</sup>
IFRIC 22	Foreign Currency Transactions and Advance Consideration <sup>1</sup>
IFRIC 23 <sup>[1], [2], [3], [4], [5], [6], [7], [8], [9], [10], [11], [12], [13], [14], [15], [16], [17], [18], [19], [20], [21], [22], [23], [24], [25], [26], [27], [28], [29], [30], [31], [32], [33], [34], [35], [36], [37], [38], [39], [40], [41], [42], [43], [44], [45], [46], [47], [48], [49], [50], [51], [52], [53], [54], [55], [56], [57], [58], [59], [60], [61], [62], [63], [64], [65], [66], [67], [68], [69], [70], [71], [72], [73], [74], [75], [76], [77], [78], [79], [80], [81], [82], [83], [84], [85], [86], [87], [88], [89], [90], [91], [92], [93], [94], [95], [96], [97], [98], [99], [100]</sup>	Uncertainty over Income Tax Treatments <sup>2</sup>
Amendments to IFRS 2	Classification and Measurement of Share-based Payment Transactions <sup>1</sup>
Amendments to IFRS 4	Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts <sup>1</sup>
Amendments to IFRS 9	Prepayment Features with Negative Compensation <sup>2</sup>
Amendments to IFRS 10 and IAS 28	Sale or Contribution of Assets between an Investor and its Associate or Joint Venture <sup>3</sup>
Amendments to IAS 19	Plan Amendment, Curtailment or Settlement <sup>2</sup>
Amendments to IAS 28	Long-term Interests in Associates and Joint Ventures <sup>2</sup>
Amendments to IAS 40	Transfers of Investment Property <sup>1</sup>
Amendments to IAS 28	As part of the Annual Improvements to IFRSs 2014 - 2016 Cycle <sup>1</sup>
Amendments to IFRSs	Annual Improvements to IFRSs 2015 - 2017 Cycle <sup>2</sup>



- 1 Effective for annual periods beginning on or after January 1, 2018
- 2 Effective for annual periods beginning on or after January 1, 2019
- 3 Effective for annual periods beginning on or after a date to be determined
- 4 Effective for annual periods beginning on or after January 1, 2021

## IFRS 9 Financial Instruments

IFRS 9 introduces new requirements for the classification and measurement of financial assets, financial liabilities, general accounting and impairments for financial assets.

Key requirements of IFRS 9 which are relevant to the Group are:

- All recognized financial assets that are within the scope of IFRS 9 are required to be subsequently measured at amortized cost or fair value. Specifically, debt investments that are held within a business model whose objective is to collect the contractual cash flows, and that have contractual cash flows that are solely payments of principal and interest on the principal outstanding are generally measured at amortized cost at the end of subsequent accounting periods. Debt instruments that are held within a business model whose objective is achieved both by collecting contractual cash flows and selling financial assets, and that have contractual terms that give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding, are generally measured at fair value through other comprehensive income. All other financial assets are measured at their fair value at subsequent accounting periods. In addition, under IFRS 9, entities may make an irrevocable election to present subsequent changes in the fair value of an equity investment (that is not held for trading) in other comprehensive income, with only dividend income generally recognized in the statement of profit or loss.
- With regard to the measurement of financial liabilities designated as at fair value through profit or loss, IFRS 9 requires that the amount of change in the fair value of the financial liability that is attributable to changes in the credit risk of that liability is presented in other comprehensive income, unless the recognition of the effects of changes in the liability's credit risk in other comprehensive income would create or enlarge an accounting mismatch in profit or loss. Changes in fair value attributable to a financial liability's credit risk are not subsequently reclassified to profit or loss. Under IAS 39 Financial Instruments: Recognition and Measurement, the entire amount of the change in the fair value of the financial liability designated as fair value through profit or loss is presented in profit or loss.

- In relation to the impairment of financial assets, IFRS 9 requires an expected credit loss model, as opposed to an incurred credit loss model under IAS 39. The expected credit loss model requires an entity to account for expected credit losses and changes in those expected credit losses at each reporting date to reflect changes in credit risk since initial recognition. In other words, it is no longer necessary for a credit event to have occurred before credit losses are recognized. <sup>[1]</sup><sub>[SEP]</sub>

Based on the Group's financial instruments and risk management policies as at June 30, 2018, the management of the Company anticipates the following potential impact on initial application of IFRS 9:

#### Classification and measurement

All financial assets and financial liabilities will continue to be measured on the same bases as are currently measured under IAS 39.

#### Impairment

In general, the management of the Company anticipates that the application of the expected credit loss model of IFRS 9 will result in earlier provision of credit losses which are not yet incurred in relation to the Group's financial assets measured at amortised costs and other items that subject to the impairment provisions upon application of IFRS 9 by the Group.

#### IFRS 15 Revenue from Contracts with Customers

IFRS 15 was issued which establishes a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. IFRS 15 will supersede the current revenue recognition guidance including IAS 18 Revenue, IAS 11 Construction Contracts and the related Interpretations when it becomes effective.

Under IFRS 15, an entity recognizes revenue when (or as) a performance obligation is satisfied, i.e. when 'control' of the goods or services underlying the particular performance obligation is transferred to the customer. Far more prescriptive guidance has been added in IFRS 15 to deal with specific scenarios. Furthermore, extensive disclosures are required by IFRS 15. <sup>[1]</sup><sub>[SEP]</sub>

In 2016, the IASB issued Clarifications to IFRS 15 in relation to the identification of performance obligations, principal versus agent considerations, as well as licensing application guidance. <sup>[1]</sup><sub>[SEP]</sub>

The management of the Company anticipates that the application of IFRS 15 in the future may result in more disclosures; however, the management of the Company does not anticipate that the application of IFRS 15 will have a material impact on the timing and amounts of revenue recognized in the respective reporting periods.

### IFRS 16 Leases

IFRS 16 introduces a comprehensive model for the identification of lease arrangements and accounting treatments for both lessors and lessees. IFRS 16 will supersede IAS 17 Leases and the related interpretations when it becomes effective.

IFRS 16 distinguishes lease and service contracts on the basis of whether an identified asset is controlled by a customer. Distinctions of operating leases and finance leases are removed for lessee accounting, and is replaced by a model where a right-of-use asset and a corresponding liability have to be recognized for all leases by lessees, except for short-term leases and leases of low value assets.

Under IAS 17, the Group has already recognized an asset for prepaid lease payments for leasehold lands where the Group is a lessee. The application of IFRS 16 may result in potential changes in classification of these assets depending on whether the Group presents right-of-use assets separately or within the same line item at which the corresponding underlying assets would be presented if they were owned.

In contrast to lessee accounting, IFRS 16 substantially carries forward the lessor accounting requirements in IAS 17, and continues to require a lessor to classify a lease either as an operating lease or a finance lease.

Furthermore, extensive disclosures are required by IFRS 16.

As at June 30, 2018, the Group has non-cancellable operating lease commitments of US\$2,074,196 as disclosed in note 27. A preliminary assessment indicates that these arrangements will meet the definition of a lease. Upon application of IFRS 16, the Group will recognize a right-of-use asset and a corresponding liability in respect of all these leases unless they qualify for low value or short-term leases.

In addition, the Group currently considers refundable rental deposits paid of US\$37,762 and refundable rental deposits received of US\$16,587 as rights and obligations under leases to which IAS 17 applies. Based on the definition of lease payments under IFRS 16, such deposits are not payments relating to the right to use the underlying assets, accordingly, the carrying amounts of

such deposits may be adjusted to amortised cost and such adjustments are considered as additional lease payments. Adjustments to refundable rental deposits paid would be included in the carrying amount of right-of-use assets. Adjustments to refundable rental deposits received would be considered as advance lease payments. <sup>[[L]]</sup><sub>SEP</sub> Furthermore, the application of new requirements may result in changes in measurement, presentation and disclosure as indicated above. <sup>[[L]]</sup><sub>SEP</sub> Except as described above, the management of the Company anticipates that the application of other new and amendments to IFRSs and Interpretations will have no material impact on the consolidated financial statements in the foreseeable future. <sup>[[L]]</sup><sub>SEP</sub>

## **CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY**

In the application of the Group's accounting policies, management is required to make judgements, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods

### ***Critical judgements in applying accounting policies***

The following are the critical judgements, apart from those involving estimations (see below), that management has made in the process of applying the Group's accounting policies and that have the most significant effect on the amounts recognized in the consolidated financial statements.

#### **Control over Zhejiang Boyuan Construction Co., Ltd. ("Zhejiang Boyuan")**

In order to comply with PRC laws and regulations limiting foreign ownership of or imposing conditions on holding National Class I Construction Qualification in the PRC, the Group operates its business through Zhejiang Boyuan by means of Contractual Arrangement (as defined below).

Management of the Company assessed whether or not the Group has control over Zhejiang Boyuan based on whether the Group has the practical ability to direct the relevant activities of Zhejiang Boyuan unilaterally. In making their judgment, the management of the Company considered the Contractual Arrangement (as defined below).

On January 10, 2009, Zhejiang Jianyou Trading Co., Ltd. ("China Privco"), a wholly-owned PRC subsidiary of the Group, Zhejiang Boyuan and shareholders of Zhejiang Boyuan, entered into a

series of agreements (the “Contractual Arrangement”). Mr. Shou Cailiang (“Mr. Shou”), the ultimate controlling shareholder, CEO and director of the Company, holds 90% equity interest in Zhejiang Boyuan.

The key provisions of the Contractual Arrangement are follows:

- (i) *Exclusive Option Agreement:* China Privco can acquire the equity interest in, and all or part of the assets and business of, Zhejiang Boyuan at any time if legally permitted at a minimal amount;
- (ii) *Management Agreement:* Zhejiang Boyuan entrusted China Privco to manage and operate the business of Zhejiang Boyuan. China Privco will be remunerated with the net earnings before tax of Zhejiang Boyuan and will assume all operational risks and bear all losses of Zhejiang Boyuan;
- (iii) *Shareholder's Voting Proxy Agreement:* The shareholders of Zhejiang Boyuan granted the right to exercise all of the voting rights of Zhejiang Boyuan to China Privco; and
- (iv) *Share Pledged Agreement:* The shareholders of Zhejiang Boyuan pledged all of the shares of Zhejiang Boyuan they own to China Privco to guarantee their obligations under Exclusive Option Agreement, Management Agreement and Shareholder's Voting Proxy Agreement.

Management of the Company, after consulting legal opinion, are of the view that the terms of the Contractual Arrangement have in substance enabled China Privco to have power over Zhejiang Boyuan, rights to variable returns from its involvement with Zhejiang Boyuan, and has the ability to use its power to affect its returns, despite the absence of formal legal equity interests held by the Group therein. Accordingly, Zhejiang Boyuan is accounted for as a consolidated structured entity and as a subsidiary of the Company.

In the opinion of the management of the Company, with reference to opinion of legal counsel, the Contractual Arrangement is in compliance with existing PRC laws and regulations, are valid, binding and enforceable, and do not result in any violation of PRC laws or regulations currently in effect in all material respects. However, uncertainties in the PRC legal system could cause the Group's current contractual arrangement structure to be found in violation of any existing and/or future PRC laws or regulations and could limit the Company's ability, through China Privco, to enforce its rights under the Contractual Arrangement.

Substantially all of the operation of the Group is carried out through Zhejiang Boyuan. If the current structure or any of the Contractual Arrangement were found to be in violation of any existing or future PRC law, the Group may be subject to penalties, which may include but not be limited to, the cancellation or revocation of the Group's business and operating licenses, being required to restructure the Group's operations or discontinue the Group's operating activities. The imposition of any of these or other penalties may result in a material and adverse effect on the Group's ability to conduct its operations. In such case, the Group may not be able to operate or control Zhejiang Boyuan, which may result in its deconsolidation.

### ***Key sources of estimation uncertainty***

The following are the key assumptions concerning the future, and other key sources of estimation uncertainty at the end of the reporting period that may have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

#### Construction contracts

Revenue recognition on a project is dependent on management's estimation of the total outcome of the construction contract, as well as the work done to date. The Group reviews and revises the estimates of contract revenue, contract costs, variation orders and contract claims prepared for each construction contract as the contract progresses. Budgeted construction revenue is determined in accordance with the terms set out in the relevant contracts. Budgeted construction costs are prepared by the management on the basis of quotations from time to time provided by the suppliers or vendors involved and the experience of the management. In order to keep the budget accurate and up-to-date, the management conducts periodic reviews of the management budgets by comparing the budgeted amounts to the actual amounts incurred. Construction revenue, construction costs and unbilled revenue include amounts derived using the percentage of completion method applied to construction contracts. Percentage of completion is calculated based on the costs incurred on each construction contract at the end of the respective accounting period divided by the total estimated costs for the contract and then multiplied by the estimated construction revenue expected to be earned.

A considerable amount of judgement is required in estimating the total contract revenue, contract costs, variation orders and contract claims which may have an impact in terms of percentage of completion and profit recognised for each job.

#### Impairment of accounts receivable and unbilled revenue

On assessing any impairment of the Group's accounts receivable and unbilled revenue, management regularly reviews the recoverability, creditworthiness of customers and ages of accounts receivable and unbilled revenue. Impairment on accounts receivable and unbilled revenue is made based on estimation of the future cash flows discounted at the original effective interest rates. If the financial condition of the customers of the Group deteriorates, resulting in an impairment of their ability to make payments, additional impairment may be required.

#### Expected timing of collections of accounts receivable and unbilled revenue

The Group classifies its accounts receivable and unbilled revenue as current and non-current assets based on the expected timing of collections of cash. This determination requires significant judgement and is based on the characteristics of each customer, contract terms and past repayment record.

## RELATED PARTY BALANCES AND TRANSACTIONS

Related parties transactions are summarized as follows:

	June 30, 2018	June 30, 2017
	\$	\$
Due from a company controlled by Mr. Shou Cailiang ("Mr. Shou"), the Chairman and Chief Executive Officer ("CEO")	56,441	55,139
Due from shareholders	755,233	-

The balances are unsecured, interest-free and repayable on demand.

Due from shareholders represented cash advanced to the shareholders, for placement into a bank to secure a bank loan granted to the Group during the current year.

The Group also had guarantees provided by related parties at the end of the reporting period shown in note 12 to the consolidated financial statements.

## SUMMARY OF QUARTERLY RESULTS

The following table is a summary of the Company's selected quarterly financial information for each of the eight quarters ended June 30, 2018:

US\$'000 (except EPS)	Revenue	Net Income (Loss)	Basic EPS	Diluted EPS
Q4, FY2018	83,845	3,218	0.13	0.10
Q3, FY2018	113,635	2,900	0.11	0.10
Q2, FY2018	66,538	256	0.01	0.01
Q1, FY2018	61,909	2,347	0.09	0.08
Q4, FY2017	46,958	326	0.01	0.01
Q3, FY2017	62,085	2,406	0.09	0.08
Q2, FY2017	60,757	1,426	0.06	0.06
Q1, FY2017	29,714	470	0.02	0.02

## LIQUIDITY AND CAPITAL RESOURCES

US\$'000	Q4, FY2018	Q4, FY2017	FY2018	FY2017
Operating activities	(4,716)	10,395	(5,519)	16,923
Investing activities	(1,027)	1,274	(2,911)	6,663
Financing activities	9,139	(10,251)	11,629	(21,194)
Effect of currency translation	(325)	49	42	(21)
Net increase in cash and cash equivalents	1,462	1,467	3,241	2,371

Net cash used in operating activities was \$5.5 million and \$4.7 million for the FY2018 and Q4, FY2018 respectively, as compared to net cash provided of \$16.9 million and \$10.4 million in the same periods last year. The change in unbilled revenue was the main driver for the substantial change in cash provided/(used) between these periods. It is mainly due to more construction projects started near the year-end and more unbilled revenue was recognised awaiting customers to settle.

Net cash used in investing activities was \$2.9 million in FY2018 and \$1.0 million for the last quarter of FY2018. For the same periods last year, the net cash provided were \$6.7 million and \$1.3 million, respectively. The major reason is due to more borrowings had been raised by the Company during the year which required more placement of restricted cash.

Net cash provided from financing activities was \$11.6 million and \$9.1 million in FY2018, and Q4, FY2018 respectively, as compared to net cash used of \$21.2 million and \$10.3 million in the same periods last year. The changes in net cash from financing activities in these periods were mainly due to the increase in bank notes payable in the periods.

The Company intends to use cash generated from operations to fund working capital requirements. The Company also intends to aggressively pursue customers for payments of unbilled revenue and overdue accounts receivable. The Company will obtain long and/or short term financing from local PRC banks or make other lending arrangements in order to subsidize any shortfall in working capital requirements in case of the cash generated from operations is not sufficient. The Company may also look to the market to issue shares or debentures in order to fund any cash shortages.

The Company's actual cash receipts from customers for the FY2018 was \$316 million. The Company also has approximately \$91 million of banking facilities of which approximately \$84 million has been used at the moment. The Company is constantly looking for additional banking facilities, and currently discussing with several local financial institutions to obtain additional facilities.

The Company's objectives when managing capital are:

- to safeguard the Company's ability to continue as a going concern, so that it can continue to provide returns for shareholders and benefits for other stakeholders, and



- to provide an adequate return to shareholders through expansion and acquisition correspondingly to the level of risk.

The Company sets the amount of capital in proportion to risk. The Company manages the capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of the underlying assets. In order to maintain or adjust the capital structure, the Company may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares, or sell assets to reduce debt.

The Company is subject to externally imposed capital requirements through its restricted cash and bank loan requirements. In addition the PRC law requires the Company to set aside a statutory reserve. Statutory reserve refers to the amount appropriated from the retained earnings in accordance with laws or regulations, which can be used to recover losses and increase capital, as approved, and, are to be used to expand production or operations. PRC laws prescribe that an enterprise operating at a profit must appropriate, on an annual basis, from its earnings an amount to the statutory reserve to be used for future company development. Such an appropriation is made until the reserve reaches a maximum equalling 50% of the enterprise's capital.

The Company's primary sources of funding have been short-term loans from banks, Secured and Unsecured Debentures, equity offerings, and cash provided by operating activities. The Company's primary uses of funding have been to provide working capital to the Company's construction projects.

The Company had cash and cash equivalents balance of \$7.2 million, \$210.3 million in current assets and \$157.0 million in current liabilities as at June 30, 2018.

On November 1, 2010, the Company completed a prospectus offering of 15,000 unsecured subordinated convertible debentures at a price of \$987 (Cdn\$1,000) per debenture for gross proceeds of \$14,799,000 (Cdn\$15,000,000). Each convertible debenture bears interest at a rate of 10% per annum to be paid semi-annually in arrears and will be due on October 31, 2015. Each convertible debenture, at the election of the holder, is convertible to 384.6153 common shares of the Company at a conversion price of Cdn\$2.60 per share. The convertible debentures are redeemable by the Company at any time from and after November 1, 2013 at a price equal to the principal amount thereof plus accrued and unpaid interest if the common shares of the Company trade at a volume weighted average price not less than 125% of the conversion price of the debentures for the 20 most recent trading days with at least 1,000 shares traded in each trading day ending five trading days before the applicable redemption notice.

On July 1, 2015, the Company amended its Unsecured Debentures with the following principal amended terms:

- (i) interest rate was increased to 11.5% from 10.0% on and from July 1, 2015;
- (ii) Debenture holders were provided with a retraction right to require the Company to repurchase Debentures on each of October 31, 2015 (up to Cdn\$5 million), October 31, 2016 (up to Cdn\$1.5 million) and October 31, 2017 (up to Cdn\$1.5 million);
- (iii) conversion price was decreased from Cdn\$2.60 to Cdn\$1.00 per share of the Company;

- (iv) maturity date of the Debentures was extended from October 31, 2015 to October 31, 2018; and
- (v) the restricted redemption period was extended to October 31, 2016.

Prior to October 31, 2016, the convertible debentures are redeemable at the issuer's option at principal amount plus accrued and unpaid interest on not less than 30 days and not more than 60 days' notice in case the current market price of the Company's shares on the date on which the notice of redemption is given is not less than 125% of the conversion price. On and after October 31, 2016, the convertible debentures are redeemable at the issuer's option not less than 30 days and not more than 60 days' prior notice at principal amount plus accrued and unpaid interest.

On October 31, 2017, 2016 and 2015, the Company completed the retraction of \$1,139,125 (Cdn\$1,500,000), \$1,155,446 (Cdn\$1,500,000) and \$3,859,216 (Cdn\$5,000,000) aggregate principal amount of its Unsecured Debentures, respectively.

On January 3, 2017, 3 unsecured subordinated convertible debentures amount to \$2,311 (Cdn\$3,000) were converted into 3,000 common shares with the conversion price of Cdn\$1.00 per share, in which the relevant amount had been released from convertible debentures equity reserve and liability of convertible debentures.

## **OUTSTANDING SHARE DATA**

As of the date of this MD&A, the Company has 25,423,065 common shares outstanding. The Company has Unsecured Debentures outstanding of Cdn\$6,997,000 that can be converted into 6,997,000 common shares. The outstanding share options granted to directors and officers are 1,755,000.

## **OFF BALANCE SHEET ARRANGEMENTS**

As at June 30, 2018, the Company had no off balance sheet arrangements such as guaranteed contracts, contingent interests in assets transferred to an entity, derivative instrument obligations or any instruments that could trigger financing, market or credit risk to the Company.

## **FINANCIAL INSTRUMENTS**

### ***Interest rate risk management***

The Group is exposed to fair value interest rate risk in relation to fixed-rate loans. The Group is also exposed to cash flow interest rate risk in relation to variable-rate bank balances and loans.

The Group does not currently hold any financial instruments that mitigate these risks. Unfavourable changes in the applicable interest rate may result in an increase in interest expense.

The Group's cash flow interest rate risk is mainly concentrated on the fluctuation of prime rate in China arising from the Group's loans disclosed in note 12 to the consolidated financial statements.

### *Sensitivity Analysis*

The sensitivity analysis has been determined based on the exposure to interest rate risk for variable-rate bank balances and loans. The analysis is prepared assuming the financial instruments outstanding at the end of the reporting period were outstanding for the whole year and all other variables were held constant.

#### *Bank balances*

If interest rates had been 100 basis points (June 30, 2017: 100 basis points) higher/lower and all other variables were held constant, the Group's post-tax profit for the year would increase/decrease by approximately \$118,000 (June 30, 2017: increase/decrease in the Group's post-tax profit of approximately \$81,000). This is mainly attributable to the Group's exposure to interest rates on its variable-rate bank balances.

#### *Borrowings*

If interest rates had been 100 basis points (June 30, 2017: 100 basis points) higher/lower and all other variables were held constant, the Group's post-tax profit for the year would decrease/increase by approximately \$373,000 (June 30, 2017: decrease/increase in the Group's post-tax profit of approximately \$246,000). This is mainly attributable to the Group's exposure to the interest rates on its variable-rate loans.

### *Credit risk management*

The Group's maximum exposure to credit risk which will cause a financial loss to the Group due to failure to discharge an obligation by the counterparties is arising from the carrying amounts of the respective recognized financial assets as stated in the consolidated statements of financial position and financial guarantees provided by the Group as disclosed in note 23 to the consolidated financial statements.

Credit risk from accounts receivable, unbilled revenue and deposits to customers encompasses the default risk of customers and non-performance by customers in accordance with contractual terms. The Group's customers are for the most part, private companies located in the PRC. Its exposure to credit risk with its customers is influenced mainly by the individual characteristics of each customer. The Group's exposure to credit risk associated with its accounts receivable, unbilled revenue and deposits to customers are the risk that a customer will be unable to pay amounts due to the Group. In its determination of valuation of accounts receivable, unbilled revenue and deposits to customers, including the allowance for doubtful accounts, management relies on current customer information and its planned course of action as well as assumptions about business and economic conditions in the future period over which the receivables are collectible. Allowances are provided for potential losses that have been incurred at the end of the reporting period. The amounts disclosed on the statements of financial position are net of these allowances for doubtful debts. Accounts receivables, unbilled revenue and deposits to customers are considered for impairment on a case-by-case basis when they are past due or when objective evidence is received that a customer will default.

Management takes into consideration the customer's payment history, the credit worthiness and the current economic environment in which the customer operates to assess impairment. Management,

on an ongoing basis, monitor the level of accounts receivable, unbilled revenue and deposits to customers attributable to each customer and the length of time taken for amounts to be settled and where necessary, takes appropriate action to follow up on those balances considered overdue.

Under PRC regulations, a general contractor is entitled to first claim against assets of its customers subject to certain conditions, which gives a general contractor a "mechanic lien" senior to all other secured debt including bank loans, bank notes and any payables. If a customer defaults on the payment on the contract with the Group, the customer can be liable to surrender the real estate property and the land use rights associated with the real estate property that is under construction.

In this regard, the directors of the Company consider that the Group's credit risk in relation to the accounts receivable and unbilled revenue are significantly reduced.

The management of the Company consider that the Group has adequate credit control for determination of credit limits, credit approvals and other monitoring procedures to ensure that follow-up actions are taken to recover overdue debts. In addition, the Group reviews the recoverable amount of each individual trade debt and unbilled revenue accounts at the end of each reporting period to ensure that adequate impairment losses are made against the irrecoverable amounts.

As of June 30, 2018, revenue from the three customers accounted for 22% (June 30, 2017: 20%) of total revenue. The outstanding amounts owed by top three accounts receivable and unbilled revenue accounted for 42% and 25% (June 30, 2017: 34% and 37%) of the total accounts receivable and unbilled revenue, respectively.

Based on management's assessment, there are no changes in the credit quality of the remaining customers. They are customers with long trading history with the Group and no default payment, the credit risk from these customers is mitigated.

The Group's bank balances and restricted cash are held in large PRC and Hong Kong banks. These assets have low credit risk due to the financial strength and credibility of the banks.

The Group had concentration of credit risk by geographical locations as all the accounts receivable and unbilled revenue are located in the PRC as at June 30, 2018 and 2017.

### ***Foreign currency risk management***

The Group has limited foreign currency exposure as the amounts of foreign currency monetary assets and liabilities held by the Group at the end of the reporting date are minimal. The management conducts periodic review of the exposure and requirements of various currencies, and will consider hedging significant foreign currency exposures should the need arise.

### ***Liquidity Risk management***

Liquidity risk is the risk that the Group is not able to meet its financial obligations as they fall due. The Group's approach to managing liquidity risk is to ensure that sufficient cash and credit facilities are available to meet liabilities when due. The contractual maturities of the Group's other loans and convertible debentures are described in notes 14 and 15 in the notes to the consolidated financial statements. The remaining financial liabilities, consisting of bank loans, bank notes payable and

accounts payable, are expected to be realized within one year. Their carrying value on the consolidated statements of financial positions are stated as undiscounted cash flow based on the earliest date on which the Group can be required to satisfy the liabilities.

The table represents undiscounted cash flow for current and non-current portion of financial liabilities as at June 30, 2018 and 2017. The undiscounted cash flow includes both interest and principal cash flows. For other financial liabilities, all balances are due within 1 year and the undiscounted cash flows are approximated to the carrying amount. To the extent that interest flows are floating rate, the undiscounted amount is derived from interest rate at the end of the reporting period:

	Weighted average <u>interest</u> <u>rate</u>	Less than <u>1 year</u>	1-2 <u>years</u>	2-5 <u>years</u>	Total undiscounted <u>cash flows</u>	Carrying <u>amount</u>
	%	\$	\$	\$	\$	\$

#### At June 30, 2018

Borrowings	5.8	76,174,290	-	-	76,174,290	75,299,783
Accounts and other payables	-	11,341,264	-	-	11,341,264	11,341,264
Bank notes payable	1.9	24,586,329	-	-	24,586,329	24,421,208
Other loans	-	643,698	-	-	643,698	643,698
Convertible debentures	33.8	5,521,927	-	-	5,521,927	5,262,463
Financial guarantee contracts (Note)	-	21,901,752	-	-	21,901,752	350,460
		140,169,260	-	-	140,169,260	117,318,876

	Weighted average <u>interest</u> <u>rate</u>	Less than <u>1 year</u>	1-2 <u>years</u>	2-5 <u>years</u>	Total undiscounted <u>cash flows</u>	Carrying <u>amount</u>
	%	\$	\$	\$	\$	\$

#### At June 30, 2017

Borrowings	4.9	67,610,134	-	-	67,610,134	66,776,845
Accounts and other payables	-	7,840,422	-	-	7,840,422	7,840,422

Bank notes payable	2.0	10,988,159	-	-	10,988,159	10,882,557
Other loans	-	3,769,693	8,420	-	3,778,113	3,778,113
Convertible debentures	33.8	1,820,313	5,601,043	-	7,421,356	5,202,812
Financial guar contracts						
(Note)	-	30,574,451	-	-	30,574,451	1,736,706
		122,603,172	5,609,463	-	128,212,635	96,217,455

Note: The amounts included above for financial guarantee contracts are the maximum amounts the Group could be forced to settle under the arrangement for the full guaranteed amount if that amount is claimed by the counterparty to the guarantee. Based on expectations at the end of the reporting period, the Group considers that it is more likely than not that such an amount will not be payable under the arrangement. However, this estimate is subject to change depending on the probability of the counterparty claiming under the guarantee which is a function of the likelihood that the financial receivables held by the counterparty which are guaranteed suffer credit losses.

### ***Economic, political, & legal risk***

The Company's operations in the PRC are subject to special considerations and significant risks not typically associated with companies in North America and Western Europe. These include risks associated with, among others, the political, economic and legal environment and foreign currency exchange. The Company's results may be adversely affected by changes in the political and social conditions in the PRC, and by changes in governmental policies with respect to laws and regulations, anti-inflationary measures, currency conversion, remittances abroad, and rates and methods of taxation, among other things.

The real estate industry in China is subject to government regulations. Until 2009, the real estate markets in a number of major cities in China had experienced rapid and significant growth. Before the global economic crisis hit all the major economies worldwide in 2009, the PRC government had adopted a series of measures to restrain what it perceived as unsustainable growth in the real estate market. From 2003 to 2013, the PRC government introduced a series of specific administrative and credit-control measures including, but not limited to, setting minimum down payment requirements for residential and commercial real estate transactions, limiting availability of mortgage loans, and tightening governmental approval process for certain real estate transactions. Such measures and policies by the government have negatively affected the real estate market and caused a reduction in transactions in the real estate market. While these measures and policies remain in effect, they may continue to depress the real estate market, dissuade would-be buyers from making purchases, reduce transaction volume, cause a decline in average selling prices, and prevent developers from raising the capital they need and increase developers' costs to start new projects. This naturally has a negative impact on the construction industry, particularly on gross margins and payment terms for new construction projects. These factors may materially and adversely affect our business, financial condition, results of operations and prospects. Despite the recent government measures aimed at maintaining the long-term stability of the real estate market, there is no assurance that the PRC

government will not continue to adopt new measures in the future that may result in short-term downward adjustments and uncertainty in the real estate market.

## **DISCLOSURE CONTROLS AND PROCEDURES AND INTERNAL CONTROLS OVER FINANCIAL REPORTING**

The **Chief Executive Officer (“CEO”)** and Chief Financial Officer (“**CFO**”) are responsible for designing disclosure controls and procedures (“**DC&P**”) and internal controls over financial reporting (“**ICFR**”) as defined in National Instrument 52-109. The control framework used in the design of both DC&P and ICFR is the internal control integrated framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

Management does not expect the Company’s disclosure controls and internal controls can prevent all errors or fraud. Due to the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all controls issues have been detected. A control system, no matter how well conceived or operated, can only provide reasonable, not absolute, assurance that the objectives of the control system are met.

The design and effectiveness of internal controls over financial reporting was assessed as of June 30, 2018. Based on the evaluation, the Company concluded that the design and effectiveness of the Company’s DC&P and ICFR was sufficiently effective to provide reasonable assurance that material information relating to the Company is made known to management and disclosed in accordance with applicable securities regulations.

## **OUTLOOK**

The continued growth of China's middle class and the ongoing development of tier two cities as a result of urbanization suggest that higher demand for the Company's construction services will remain strong in the long term. In the near term, the restrictive measures imposed by the central government on the residential market and the tightening of financing facilities to property developers will continue to dampen the pace of growth for the Company. Over the longer term, the Company believes that its growth will be driven by expanding its reach in tier-two cities and increasing focus on speciality construction projects, which the Company believes will deliver higher profit margins. As a part of this strategic direction, the Company plans to upgrade its qualification and engineering standards to ensure that it can tap into this growing market potential.

## **CORPORATE DIRECTORY**

### **Management**

Shou Cailiang  
*Chairman, President & Chief Executive Officer*

Paul Law  
*Chief Financial Officer*

Shu Ren  
*Secretary*

### **Board of Directors**

Shou Cailiang  
*Chairman, Director, President & Chief Executive Officer*

Francis Leong  
*Lead Director*

Manhong Liu  
*Director*

John (Jack) Duffy  
*Director*

Dr. Fan Lixin  
*Director*

Shu Ren  
*Director and Secretary*

Tang Wei  
*Director and Vice President*

### **Corporate Office**

Boyuan Construction Group, Inc.  
Jinhui Plaza, 500 Matang Road  
Jiaxing Economic Development Zone  
Jiaxiang, Zhejiang, China 314000

### **Auditors**

Deloitte Touché Tohmatsu  
Hong Kong

### **Transfer Agent**

Computershare Trust Company of Canada  
600, 530 – 8th Avenue SW  
Calgary, Alberta  
T2P 3S8

### **Stock Exchange Listing**

Toronto Stock Exchange  
Symbol: BOY, BOY.DB.A