

# INDEPENDENT AUDITOR'S REPORT

TO THE MEMBERS OF CHINA ENVIRONMENT LTD.  
FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2015

## Report on the Financial Statements

We were engaged to audit the accompanying financial statements of China Environment Ltd. (the "Company") and its subsidiaries (the "Group") which comprise the statements of financial position of the Group and the Company as at 31 December 2015, and the consolidated statement of profit or loss and other comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows of the Group and the statement of changes in equity of the Company for the year then ended, and a summary of significant accounting policies and other explanatory information.

### *Management's Responsibility for the Financial Statements*

Management is responsible for the preparation of financial statements that give a true and fair view in accordance with the provisions of the Singapore Companies Act, Chapter 50 (the "Act") and Singapore Financial Reporting Standards, and for devising and maintaining a system of internal accounting controls sufficient to provide a reasonable assurance that assets are safeguarded against loss from unauthorised use or disposition; and transactions are properly authorised and that they are recorded as necessary to permit the preparation of true and fair profit and loss accounts and balance sheets and to maintain accountability of assets.

### *Auditor's Responsibility*

Our responsibility is to express an opinion on these financial statements based on conducting the audit in accordance with Singapore Standards on Auditing. Because of the matters described in the *Basis for Disclaimer of Opinion* paragraphs, however, we were not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

### *Basis for Disclaimer of Opinion*

#### (1) Opening balances

Our independent auditor's report dated 26 April 2019 on the revised financial statements for the financial year ended 31 December 2014 ("FY 2014") contained a disclaimer of opinion. The basis for disclaimer of opinion in our Auditor's Report on the previously issued FY 2014 financial statements audited by Baker Tilly TFW LLP, the auditor's report which is dated 1 April 2015, is disclosed in Note 37 to the financial statements.

In view of the matters described in the basis for disclaimer of opinion paragraphs on the financial statements for FY 2014, we were unable to determine whether the opening balances as at 1 January 2015 were fairly stated.

Since the opening balances as at 1 January 2015 are entered into the determination of the financial position of the Group and of the Company as at 31 December 2015 and of the financial performance, changes in equity and cash flows of the Group and changes in equity of the Company for the financial year ended 31 December 2015, we were unable to determine whether adjustments, if any, might have been found to be necessary in respect of the Group's and the Company's financial statements for the financial year ended 31 December 2015 - in view of brought forward implications of the prior year balances.

Accordingly, our opinion on the current financial year's financial statements of the Group and the Company is also modified because of the implications and possible effects of these matters that might bear on the comparability and/or lack of comparability of the current year's figures and the corresponding figures.

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## Report on the Financial Statements (Cont'd)

### *Basis for Disclaimer of Opinion (Cont'd)*

#### (2) Existence and Recoverability of Trade and Bill Receivables

As disclosed in Note 37(2)(ii) and (iii), we have performed debtors' circularisation of 5 major trade receivables amounting to RMB 636,576,000 (comprising approximately 79.19% of the Group's total trade receivables as at 31 December 2015 before impairment and after restatement adjustment) to ascertain their existence. The audit response from the circularised confirmation from the 5 debtors did not reveal any exceptions, that is, the circularised balances were affirmed without exceptions.

However, based on our unannounced site visits to the offices of the 5 major trade receivables on 17 and 18 November 2016, and 28 and 29 of December 2016, we were unable to verify the confirmations received from all the 5 major debtors. These 5 major trade debtors are from the books of the subsidiary, Fujian Dongyuan Environmental Protection Co., Ltd. ("FJDY"). The details of our findings are disclosed in Notes 36 (iii) and (iv).

As at 31 December 2015, the Group's net total trade receivables amounted to RMB 12,288,000. This is after an impairment loss of RMB 636,576,000 for the 5 major trade receivables and an additional impairment loss of RMB 155,028,000 made by the current Board of Directors ("Current Board"). The additional impairment loss comprised RMB 152,516,000, RMB 1,730,000, RMB 731,000 and RMB 51,000 pertaining to those trade receivables in the books of the subsidiaries FJDY, Anhui Dongyuan Environmental Protection Co., Ltd ("AHDY"), Xiamen Gongyuan Environmental Protection Technology Co., Ltd ("XMDY") and Gates Engineering Pte. Ltd. respectively, where there were no subsequent receipts at the date of this Report.

However, included in the Group's trade receivable balance of RMB 12,288,000 as at 31 December 2015, there are no impairment loss being recorded for trade receivables amounting to RMB 1,950,000 in the books of the subsidiary, FJDY, where there were no subsequent receipts at the date of this Report. Accordingly to management of the Current Board, management is confident that the sum of RMB 1,950,000 is recoverable as management has been negotiating with the debtor for payment.

Consequently, we were not able to ascertain the recoverability of the amount of RMB 1,950,000 in the Group's trade receivables of RMB 12,288,000 (for which there are no subsequent receipts as at the date of this Report) nor are we able to determine the validity of recording certain trade receivables.

#### (3) Revenue, Costs of Sales, Value Added Tax ("VAT") and Trade Payables and Trade Receivables

As discussed in Point 2 of our Report above, and as stated in Notes 36 (iii) and (iv) to the financial statements, in view of the lack of on-site evidence to establish the existence of the 5 major trade receivables, we are unable to ascertain whether the Group's revenue and the costs of sales amounting to approximately RMB 36.66 million and 23.32 million respectively are valid and appropriately stated.

In performing the audit of AHDY and FJDY, we compared the VAT forms, submitted by management of the former Board of Directors ("Former Board") for FY 2015, to the Tax Bureau website printout furnished by management of the Current Board. We noted that the submitted VAT forms were overstated by approximately RMB 2.30 million and RMB 34.76 million respectively. By inference, this could possibly imply that the revenues for AHDY and FJDY are overstated by approximately RMB 13.53 million and RMB 204.47 million, respectively, based on 17% VAT tax rate.

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## Report on the Financial Statements (Cont'd)

### *Basis for Disclaimer of Opinion (Cont'd)*

#### (3) Revenue, Costs of Sales, Value Added Tax ("VAT") and Trade Payables and Trade Receivables (Cont'd)

Accordingly, we were unable to ascertain the accuracy and appropriateness of the carrying amounts of the trade payables and VAT payables, which amounted to approximately RMB 15.65 million as at 31 December 2015, as stated in Note 23.

Furthermore, due to the above-mentioned matters and the limitations and findings mentioned in Point 2 of our Report, we were unable to determine the validity, accuracy and appropriateness of the carrying amounts of the trade receivables totalling RMB 12,288,000 as at 31 December 2015, as stated in Note 18.

#### (4) Investment in subsidiaries and associated company

As stated in Notes 14 and Note 15 to the financial statements, the Group's carrying amount of its 49% owned associated company, Beijing Gongdao Environmental Protection Technology Co., Ltd ("BGDEPT") and the Company's carrying amount of its four subsidiaries as at 31 December 2015 amounted to approximately RMB 2.45 million and RMB 665 million respectively.

In view that all the Company's subsidiaries are currently not in operation, management of the Current Board is unable to carry out a review of the recoverable amount of the investment in subsidiaries companies despite indications of impairment. Accordingly, we were unable to obtain sufficient appropriate audit evidence to determine the appropriateness of the carrying amounts of the investment in the subsidiaries.

For investment in the associated company, BGDEPT, management of the Current Board is unable to obtain the necessary accounting records and information necessary from management of BGDEPT for the assessment of the recoverable amount of the associate company. Accordingly, we were unable to obtain sufficient appropriate audit evidence to determine the appropriateness of the carrying amounts of the investment in the associated company, BGDEPT.

In addition, in the process of performing our audit verification of, based on work done to verify the equity interest in BGDEPT, management of the Current Board upon our inquiry, discovered that the Group's actual equity interest held in BGDEPT should be 83% instead of the 49% - as indicated in the audited financial statements for FY 2013 and FY 2014 by the predecessor auditor.

However, the Current Board is unable to determine whether the 83% held equity investment in BGDEPT would constitute an element of control. Control is defined as being exposed to, or has the rights to, variable returns from the Group's involvement in BGDEPT and has the ability to affect those returns through its power over BGDEPT. To be conservative, the Current Board has decided not to reclassify the investment from associated company to investment in subsidiaries.

Consequently, we were unable to carry out alternative audit procedures to determine the appropriateness of the classification of the investment in BGDEPT by the Current Board.

As stated in Note 36 (xiii), on 31 July 2018, the Company announced that BGDEPT is under voluntary liquidation. On 29 March 2019, the Company announced that BGDEPT has completed its deregistration process.

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## Report on the Financial Statements (Cont'd)

### *Basis for Disclaimer of Opinion (Cont'd)*

#### (5) Inventories

As stated in Note 16, as at 31 December 2015, the Group's inventories had a carrying amount of RMB 8,135,000. We were unable to obtain any sufficient appropriate supporting documents, information and explanations that we considered necessary to ascertain if the inventories were properly carried at the lower of its cost and its net realisable value. This is because management from the Former Board is unable to furnish us with the required supporting documents and explanations.

#### (6) Proceeds from placement of 72,500,000 new ordinary shares

As stated in Note 29, on 7 January 2015, the Company announced the completion of the placement of 72,500,000 warrants and 72,500,000 new ordinary shares of S\$0.104 each ("Placement"). Following completion of the Placement, the total number of issue ordinary shares of the Company increased from 735,520,646 shares to 808,020,646 shares. The new shares rank *pari passu* in all respects with existing ordinary shares of the Company.

The 72,500,000 unlisted warrants were allotted to the subscriber. These warrants granted the right to the subscriber to subscribe for one new share for each warrant (i.e. total 72,500,000 shares) (the "Warrant Shares") at the issue price of S\$0.104 per Warrant Share, for an aggregate amount of S\$7,540,000. The warrants may be exercised in whole by the subscriber at any time, no later than the date falling 18 months from the issue date of the warrants. The warrants had since expired at the date of this Report (Note 29).

Following completion of the placement of 72,500,000 new ordinary shares, an amount of S\$7,540,000 (being the proceeds of the placement of 72,500,000 new ordinary shares) was collected and the Company transferred S\$6,000,000 (equivalent to RMB 27,858,000) to its subsidiary, XMGY on 12 January 2015 as reflected in the Company's bank statement. Upon receipt of RMB 27,858,000, we noted, from journal entries recorded in XMGY that a payment of RMB 25,000,000 was made to its supplier, Bengbu Xingyuan Environmental Protection Technology Co., Ltd ("BBXY") on 16 January 2015 as settlement of outstanding balance for purchases. According to management of the Former Board, this payment is based on suppliers' contracts signed on May 2015 instead of suppliers' invoices. We have verified this payment from XMGY to BBXY to the bank advice. We were informed by management of the Former Board that this amount was later transferred to a customer of FJDY, Shanxi Electric [see also Note 36 (iv)] by BBXY resulting in amount of RMB 25 million due from FJDY as reflected in XMGY's journal entries.

However, management of the Former Board was unable to provide us with any other supporting documents for the journal entries except for those as mentioned above. Upon our further inquiry, management of the Former Board informed us that the proceeds were transferred to its fellow subsidiary, FJDY and the journal entries reflecting the transfer from XMGY to BBXY, and later to Shanxi Electric, was an error. We are unable to verify this representation from the Former Board.

As management of the Former Board was unable to provide us with the bank statements of FJDY that shows the RMB 25 million was transferred from XMGY nor any other supporting documents to verify on the representation made by management of the Former Board, we were unable to determine whether the proceeds had eventually reached the bank account of FJDY. Accordingly, we were unable to conclude whether the proceeds from the placement of 72,500,000 new ordinary shares of S\$0.104 each had actually reached the bank accounts of the Group and/or if the Group had benefited from the intended proceeds from the Placement.

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## Report on the Financial Statements (Cont'd)

### *Basis for Disclaimer of Opinion (Cont'd)*

#### (7) Tax Provision, Current and Deferred Tax Expense

During our audit, management of the Former Board provided a copy of all the PRC subsidiaries' tax computation that were filed with the local tax authorities. As the tax computations for FJDY and AHDY did not bear any local tax bureau company stamp, we had requested for further supporting documents and explanation from management. We did not receive a response to our request.

We were also unable to perform any alternative procedures as we were not given access by the management of the Former Board to log into the tax website to verify the tax references, particularly, the amount of the tax expenses.

Our request and queries to verify the amount of the tax expenses for FJDY and AHDY continued to be denied by management of the Former Board until the management of the Current Board took over the day-to-day operations of the Group. We finally managed to get another tax computation for FJDY from management of the Current Board that contained the local tax bureau's company stamp. Consequently, we found that the tax payable amount for FJDY to be overstated by RMB 7,780,105 due to overstated profits before tax in the management accounts.

For AHDY, we have compared the tax submission form by management of the Former Board for FY 2015 to the Tax Bureau website print out (furnished by management of the Current Board) and noted that the submitted tax submission form was overstated by approximately RMB 428,000.

For XMGY, we were allowed access to the tax website by management of the Former Board during our audit. We noted that the numbers were consistent with the tax computations that contained the local tax authority company stamp.

As management of the Current Board is unable to put through the appropriate adjustments to rectify the above discrepancies due to lack of supporting documents (as discussed in Point 8 of our Report below), we were unable to determine whether the Group's provision of taxation and tax expenses amounting to RMB 2,348,000 and RMB 2,157,000 are valid, accurate and appropriately stated.

Consequently, we were also unable to determine the correctness and appropriateness of the Group's disclosure of deferred tax balance, indicated as a zero balance, as at the end of the reporting period.

#### (8) Loss of Partial Accounting Books and Records and Supporting Documents and events occurring after the reporting period

As disclosed in Note 36(v), the current Board announced on 18 August 2017 that pursuant to the judgment obtained by China Construction Bank ("CCB") against the Company's wholly owned subsidiary FJDY, CCB is entitled to sell off the land use rights and property assets of a related company, Fujian Mintai Environmental Protection Co. Ltd ("FJMT") (owned by former executive Chairman, Mr Huang Min), which was previously pledged as security for the Group's unsecured bank borrowings of RMB 27 million [Note 26(3)]. As part of the handover requirements, the Longyan People Court in China had granted the Company personal access to FJDY's office premises on 26 July 2017, primarily to retrieve and recover FJDY's documents from the said office premises.

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## Report on the Financial Statements (Cont'd)

### *Basis for Disclaimer of Opinion (Cont'd)*

(8) Loss of Partial Accounting Books and Records and Supporting Documents and events occurring after the reporting period (Cont'd)

Upon entry into the FJDY office premises, it was discovered that the office was in a state of disarray, with evidence of being ransacked. The Company is in the process of recovering and retrieving documents from the premises. The Company made an announcement, based on its preliminary assessment, that a number of documents seem to be missing, and therefore, the records of the FJDY's various departments are unlikely to be found and/or incomplete.

In view of the missing documents, we were unable to complete the required audit procedures for events occurring after the reporting period. We consider it necessary to satisfy ourselves on the possibility of material and reportable matters that might have occurred after the reporting period, in particular, those having implications to transactions, balances and matters, recorded or unrecorded as at 31 December 2015.

Consequently, we were unable to determine whether all significant subsequent events have been adequately dealt with in these financial statements with respect to disclosures, presentation and adjusting subsequent events.

(9) Going concern and legal actions against the Group

As at 31 December 2015, the Group's current liabilities exceeded current assets by RMB 181,340,000. In addition, the Group incurred a net loss of approximately RMB 450,784,000 for the financial year ended 31 December 2015.

As at 31 December 2015, the Group has bank balances amounting to RMB 63,517,000 and this is insufficient to meet its financial obligation for its short-term borrowings which amounted to RMB 173,611,000 as at 31 December 2015.

As disclosed in Note 36 (viii), the following companies had issued letter of demand and filed Civil suits against the PRC subsidiaries subsequent to the end of the financial year:

- (i) Longyan Dongxiao Construction Engineering Co. Ltd against FJDY for a sum of RMB 1.27 million;
- (ii) Fujian Tongyong Hengxin Electrical Engineering Co. Ltd against FJDY for a sum of RMB 53,000;
- (iii) Chen Bing (Brother-in-law of Group's former Executive Chairman Mr Huang Min) against FJDY for a sum of RMB 5,000,000;
- (iv) Chen Wenzhong against FJDY for a sum of RMB 490,000;
- (v) Wuyi Jiufeng Anzhuang Engineering Co. Ltd against AHDY for a sum of RMB 817,630 and RMB 637,380; and
- (vi) Fujian Mintai Environmental Protection Co., Ltd against FJDY for a sum of RMB 3,209,712;

In addition, as disclosed in Note 36 (viii), the following banks have also taken legal actions against the PRC subsidiaries subsequent to the end of the financial year:

- (i) Bank of China Bengbu against FJDY for a sum of RMB 20 million;
- (ii) Bank of China Longyan against FJDY for a sum of approximately RMB 56 million;
- (iii) China Construction Bank against FJDY for a sum of RMB 23 million; and
- (iv) Zhongxin bank against FJDY for a sum of approximately RMB 37.2 million

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## Report on the Financial Statements (Cont'd)

### *Basis for Disclaimer of Opinion (Cont'd)*

#### (9) Going concern and legal actions against the Group (Cont'd)

The outcome of these civil suits and legal actions are disclosed in Note 36 (viii).

These civil suits and legal actions coupled with the above Points in our Report as basis for disclaimer of opinion, has created a material uncertainty with respect to the Group's cash flow management that may cast significant doubt over the Group's and the Company's ability to continue as a going concern.

As disclosed in Note 2(a) to the financial statements, the directors have prepared the financial statements on going concern basis. Based on the limited information about the Group and of the Company made available to us, we were unable to perform alternative procedures to determine the appropriateness of the use of the going concern assumption.

Apart from the above legal suits and as disclosed in Note 36(viii), the Current Board has represented that there are no new or on-going legal suits against the Group. In view of the limitation detailed in Point 8 of our Report and the change of key management, we were unable to perform any required procedures to satisfy ourselves as to whether there are any new or on-going legal suits against the Group.

### *Disclaimer of Opinion*

Because of the significance of the matters described in the Basis for Disclaimer of Opinion paragraphs, we have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, we do not express an opinion on the financial statements.

## Report on Other Legal and Regulatory Requirements

In our opinion, in view of the significance of the matters referred to in the Basis for Disclaimer of Opinion paragraphs, we do not express an opinion on whether the accounting and other records required by the Act to be kept by the Company have been properly kept in accordance with the provisions of the Act.

### **RT LLP**

Public Accountants and  
Chartered Accountants

Singapore, 9 May 2019