

INDEPENDENT AUDITOR'S REPORT

To the members of Leader Environmental Technologies Limited

Report on the Audit of the Financial Statements

Opinion

We have audited the financial statements of Leader Environmental Technologies Limited (the Company) and its subsidiaries (the Group), which comprise the consolidated statement of financial position of the Group and the statement of financial position of the Company as at 31 December 2018, 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 for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements of the Group and the statement of financial position of the Company are properly drawn up in accordance with the provisions of the Companies Act, Chapter 50 (the Act) and Singapore Financial Reporting Standards (International)(SFRS(I)s) so as to give a true and fair view of the consolidated financial position of the Group and the financial position of the Company as at 31 December 2018 and of the consolidated financial performance, consolidated changes in equity and consolidated cash flows of the Group for the year ended on that date.

Basis for Opinion

We conducted our audit in accordance with Singapore Standards on Auditing (SSAs). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are independent of the Group in accordance with the Accounting and Corporate Regulatory Authority (ACRA) Code of Professional Conduct and Ethics for Public Accountants and Accounting Entities (ACRA Code) together with the ethical requirements that are relevant to our audit of the financial statements in Singapore, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the ACRA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Material Uncertainty Related to Going Concern

We draw attention to Note 2(f) in the financial statements, which indicates that the Group incurred a loss before taxation of RMB10.4 million (2017 – profit before taxation of RMB13.4 million) and total comprehensive loss of RMB10.3 million (2017 – total comprehensive income of RMB13.4 million) during the financial year ended 31 December 2018. As of that date, the Group's current assets exceeded its current liabilities by RMB53.6 million (2017 – RMB64.0 million) while the Company's current liabilities exceeded its current assets by RMB7.2 million (2017 – RMB3.5 million) as stated in Note 2(f). The Group also incurred net cash used in operating activities of RMB11,899,000 (2017 – RMB1,943,000). These events or conditions, along with other matters as set forth in Note 2(f), indicate that a material uncertainty exists that may cast significant doubt on the Group's ability to continue as a going concern. Our opinion is not modified in respect of this matter

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Key Audit Matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial statements of the current period. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. In addition to the matter described in the Material Uncertainty Related to Going Concern section, we have determined the matters described below to be the key audit matters to be communicated in our report.

Key audit matters	Risk	Our responses and work performed
Revenue recognition for construction contracts and provision for foreseeable losses	The Group is primarily involved in the business of design and construction of environmental protection systems, primarily for industrial waste gas and wastewater treatments. We focus on revenue recognition and provision foreseeable losses because (i) the accuracy and timing of revenue recognition for construction contracts under the percentage of completion method requires the determination of the stage of completion of the project and timing of revenue recognition which involves significant management judgement and use of estimates; and (ii) when it is probable that the total contract costs would exceed the total construction revenue and remaining costs. No provision for foreseeable losses was recognised for the financial year ended 31 December 2018. The Group's disclosures about revenue recognition and contract work-in-progress are included in the significant accounting policy in Note 2(e) and Note 7 to the financial statements.	<u>Contract costs</u> We obtained an understanding of on-going contracts through discussions with management and examination of contract documentation (including correspondences with customers). In relation to actual costs incurred, we: - assessed the competence of the surveying engineers; - agreed the progress of the construction to certified progress reports from engineers; and - performed substantive testing procedures by verifying contracts costs including any variation orders to the underlying documentation. In relation to estimated total contract costs, we: - discussed with the project managers to assess the reasonableness of estimated total contract costs; - evaluated management's underlying assumptions made using our understanding of past completed projects; and - agreed the cost to complete for each contract by substantiating costs that have been committed to quotations from and contracts with suppliers. We compared the contract revenue against the estimated total contract costs. <u>Revenue</u> We have reviewed and evaluated the accounting policy on revenue recognition, taking into account the performance obligations stipulated in the sales transactions; We have performed walkthroughs of the revenue control process and tested the design and implantation of key controls identified to ascertain that key controls are operating effectively;

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Key Audit Matters (Cont'd)

Key audit matters	Risk	Our responses and work performed
Revenue recognition for construction contracts and provision for foreseeable losses		We have tested selected revenue transactions by assessing and evaluating the following steps: 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 - Identifying Performance Obligations Step 5 - Recognize revenue when (or as) the entity satisfies a performance obligation We have assessed the reasonableness of the stage of completion of the contract by verifying against internal evaluation of the progress of the contract by in-house engineers and acknowledgement by customer. We have evaluated the competency, capabilities and objectivity of a management expert (i.e. in-house engineers). We have assessed the reasonableness of the percentage of completion by cross checking using the input and output method of determining percentage of completion. We have performed arithmetic checks on the calculation of percentage of completion. We also computed the cumulative construction revenue and the construction revenue for the current financial year and agreed to the accounting records and found no exception. We also considered the adequacy of the disclosures in the financial statements, in describing the inherent degree of subjectivity and key assumptions in the estimates.

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Key Audit Matters (Cont'd)

Key audit matters	Risk	Our responses and work performed
Impairment of trade and other receivables and contract assets	The Group is subject to contract risk with significant judgment and accounting estimates used in determining the recoverability of trade and other receivables and contract assets. The Group's disclosures about revenue recognition, contract assets, trade and other receivables are included in the significant accounting policy in Note 2(e) and Notes 7 and 9 to the financial statements.	We have circularised significant trade receivable and payables balances and significant advances to suppliers. We have: - discussed with management regarding the level and ageing of receivables and recoverability of amounts due from customers, along with the consistency and appropriateness of receivables and recoverability of amounts due from customers by assessing recoverability with reference to cash received in respect of debtors and billings raised against valuation of amounts due from customers. In addition, we have considered the Group's previous experience of bad debt exposure and the individual counterparty credit risk - assessed the recoverability of overdue unprovided debt with reference to the historical levels of bad debt expense and credit profile of the counterparties - tested these balances on a sample basis through agreement to post period end invoicing, post period end cash receipt or agreement to the terms of the contract in place, as appropriate; - Considered the consistency of judgments regarding the recoverability of trade receivables made year on year through discussion with management on their rationale and obtaining evidence to support judgment areas, and - We also considered the adequacy of the disclosures in the financial statements, in describing the inherent degree of subjectivity and key assumptions in the estimates. We reviewed management's assessment of the commencement of the projects relating to the advances paid to suppliers to the underlying documentation and its recoverability if the project is subsequently cancelled. For projects which are not cancelled, we have reviewed the financial health of the suppliers to ensure that they are able to meet the needs of the specific projects.

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Key Audit Matters (Cont'd)

Key audit matters	Risk	Our responses and work performed
Impairment of trade and other receivables and contract assets (Cont'd)		We have concurred with management's assessment on the use of the simplified approach on impairment assessment on trade receivables and contract assets where management chooses as its accounting policy to measure the loss allowance at an amount equal to lifetime expected credit losses. Management has assessed the presumed default may happened for debts more than 1 year based on its historical collection pattern. Further, the expected credit loss for specialised equipment construction industry took the presumption of 3 years as indication of default. This is consistent with the accounts receivable provisioning policy where customers are not making any payment more than 1 year will be provided full provision. We have concurred with management's assessment on the use of the general approach on impairment assessment on other receivables where management determines the other receivables as 12 month expected credit loss (ECL) and lifetime ECL.
Impairment of deposits to a trade supplier	The Group is subject to contract risk with significant judgment and accounting estimates used in determining the recoverability of deposits paid to a trade supplier if the underlying project is aborted. The Group's disclosures about deposits paid to a supplier is in Note 10 to the financial statements.	The deposits to a trade supplier are made without the trade supplier invoices obtained at the point before the expenses were incurred. The deposits to a trade supplier will be reclassified and recognised as project costs upon the receipt of trade supplier invoices. Payments are made to the trade suppliers for the following reasons: - the items purchased from trade suppliers must be customised to meet the needs of specific projects. Suppliers would require advances in order to commit to the production of these customised items. - some customers impose a requirement on the project bidders to pay deposits to the customer-appointed supplier(s) during the bidding stage or upon signing of the contract so as to ensure that the Group would be capable of providing the required initial capital to facilitate timely delivery of items to project sites and to complete the project on a timely basis. In FY2018, the deposits to a trade supplier amount to RMB68,600,000 for 3 projects for the subsidiary group. The supplier is one of the top suppliers in Dunhuang which is one of the locations that the Group operates in.

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Key Audit Matters (Cont'd)

Key audit matters	Risk	Our responses and work performed
Impairment of deposits to a trade supplier (Cont'd)		We considered the potential risks and implications associated with deposits paid to this supplier and we have identified specific procedures to address these risks: a) We circularised the deposits paid to this supplier; b) We reviewed management's assessment of the commencement of the projects relating to the deposits paid to this supplier to the underlying documentation; c) For projects that are delayed and pending further discussions with the customers during the financial year, we have traced to subsequent refund of the deposit. As at the date of this report, the Group had collected a partial refund of RMB20 million from this supplier. The projects are due to long delay in the commencement of projects that have no visibilities of their commencement dates because of factors beyond the control of the Group and the customers. Factors include the requirement to clear land areas for the constructions of the wastewater treatment systems. The clearance of land requires time needed for the relocations of the people still residing in these locations that has been earmarked for the projects; d) The Group had also entered into a settlement agreement with this supplier to obtain refund of the deposits in order to further minimise its credit risk exposure. Based on the settlement agreement, the supplier is expected to repay all the deposits for projects if not materialised before the end of the financial year ending 31 December 2019. In addition, the supplier has no history of default in refund to the Group upon termination of wastewater project during the last 2 financial years. Accordingly, no expected credit loss is provided; and e) We have concurred with management's assessment on the use of the general approach on impairment assessment on deposits to this supplier where management determines the deposits to supplier as 12 month expected credit loss (ECL) and lifetime ECL. We assessed the adequacy of the related disclosures in the notes to the financial statements.

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Key Audit Matters (Cont'd)

Key audit matters	Risk	Our responses and work performed
Impairment of investment in subsidiary	Investment in subsidiary is tested for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss RMB55 million is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is based on certain key assumptions, such as cash flow projections covering a two-year period and the perpetual growth rate and discount rate per cash generating unit. These assumptions which are determined by management are judgemental.	We have identified the valuation of investment in subsidiary is significant to our audit. We considered the potential risks and implications associated with investment in subsidiary and we have identified specific procedures to address these risks: a) Reviewed for external and internal indications of impairment for its investment in subsidiary. b) Assessed if the recoverable amount of investment in subsidiary is measured as the higher of "fair value less costs of disposal" and "value in use". c) Obtained an understanding of the valuation model and assumptions used. d) Challenged management's assumption and involving independent valuation experts to support us. e) Reviewed management's cash flows forecast and assessment of value-in-use assumptions and estimates including the discount rate used for the assessment. f) Assessed the competency, capability and objectivity of the management and auditor expert and appropriateness of their work. g) Assessed the adequacy of impairment in subsidiary disclosure in the note to the financial statements. Management's disclosures on the impairment of investment in subsidiary is included in notes to the consolidated financial statements.

Other matters

The Company was placed on the watch-list pursuant to Rule 1311(2) of the SGX-ST Listing Manual since 3 March 2016 due to the Minimum Trading Price (the "MTP") Entry Criterion. Based on the assessment performed by Singapore Exchange Securities Trading Limited (the "SGX-ST") under the revised MTP rules, the Company will continue to be placed on the watch list with effect from 5 June 2017. Accordingly, the Company must take active steps to meet the requirements of Rule 1314(2) of the SGX-ST Listing Manual within 36 months from 5 June 2017 to exit the MTP watch list, failing which SGX-ST would delist the Company or suspend trading in the Company's shares with a view to delisting the Company.

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Other information

Management is responsible for the other information. The other information comprises the “Directors’ Statement” section of the annual report (but does not include the financial statements and our auditor’s report thereon), which we obtained prior to the date of this auditor’s report, and the other sections of the annual report (the Other Sections) which are expected to be made available to us after that date.

Our opinion on the financial statements does not cover the other information and we do not and will not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed on the other information that we obtained prior to the date of this auditor’s report, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

When we read the Other Sections, if we conclude that there is a material misstatement therein, we are required to communicate the matter to those charged with governance and take appropriate actions in accordance with SSAs.

Responsibilities of Management and Directors 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 Act and SFRS(I)s, 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 financial statements and to maintain accountability of assets.

In preparing the financial statements, management is responsible for assessing the Group’s ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Group or to cease operations, or has no realistic alternative but to do so.

The directors’ responsibilities include overseeing the Group’s financial reporting process.

Auditor’s Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor’s report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with SSAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

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Auditor's Responsibilities for the Audit of the Financial Statements (Cont'd)

As part of an audit in accordance with SSAs, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit 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 Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with the directors regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the directors with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with the directors, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matter. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

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Report on Other Legal and Regulatory Requirements

In our opinion, 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.

The engagement partner on the audit resulting in this independent auditor's report is Tei Tong Huat.

Foo Kon Tan LLP
Public Accountants and
Chartered Accountants

Singapore, 4 April 2019