

RECO INTERNATIONAL GROUP INC.
Consolidated Financial Statements
September 30, 2019 and 2018
(Expressed in Canadian Dollars)

MANAGEMENT'S RESPONSIBILITY FOR THE CONSOLIDATED FINANCIAL STATEMENTS

The accompanying consolidated financial statements of Reco International Group Inc. for the years ended September 30, 2019 and 2018 have been prepared by management in accordance with International Financial Reporting Standards.

The consolidated financial statements include some amounts that are based on management's best estimates and judgements and, in their opinion, present fairly the Company's financial position, results of operations and cash flows.

Management maintains systems of internal control designed to provide reasonable assurance that the assets are safeguarded, that all transactions are authorized and duly recorded, and that financial records are properly maintained to facilitate the preparation of the consolidated financial statements in a timely manner. The Board of Directors is responsible for ensuring that management fulfils its responsibilities for financial reporting and is ultimately responsible for reviewing and approving the consolidated financial statements. The Board carries out this responsibility principally through its Audit Committee.

The Audit Committee of the Board of Directors has reviewed the consolidated financial statements with management and the external auditors. RSM Alberta LLP, an independent firm of chartered professional accountants, appointed as external auditors by the shareholders, have audited the consolidated financial statements and their report is included herein.

"Hugh Zhen"
Signed
Hugh Zhen
President and Chief Executive Officer

"Quin Quang Sie"
Signed
Quin Quang Sie
Chief Financial Officer

January 28, 2020



RSM Alberta LLP

2500, Bell Tower
10104 – 103rd Avenue NW
Edmonton, Alberta T5J 0H8

O +1 780 428 1522
F +1 780 425 8189

rsmcanada.com

INDEPENDENT AUDITOR'S REPORT

To the Shareholders of Reco International Group Inc.

Opinion

We have audited the consolidated financial statements of Reco International Group Inc. (the "Company") which comprise the consolidated balance sheets as at September 30, 2019 and September 30, 2018, the consolidated statements of operations and comprehensive income (loss), changes in equity and cash flows for the years then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial positions of the Company as at September 30, 2019 and September 30, 2018, and its consolidated financial performance and its consolidated cash flows for the years ended September 30, 2019 and September 30, 2018 in accordance with International Financial Reporting Standards ("IFRS").

Basis for Opinion

We conducted our audit in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Consolidated Financial Statements* section of our report. We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the consolidated financial statements in Canada, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Other information

Management is responsible for the other information. The other information comprises the information included in the Management's Discussion and Analysis.

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

In connection with our audit of the consolidated 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 consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

THE POWER OF BEING UNDERSTOOD
AUDIT | TAX | CONSULTING

We obtained Management's Discussion and Analysis prior to the date of this auditor's report. If, based on the work we have performed, 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.

Responsibilities of Management and Those Charged with Governance for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with IFRS, 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.

In preparing the consolidated financial statements, management is responsible for assessing the Company'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 Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company's financial reporting process.

Auditor's Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated 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 Canadian generally accepted auditing standards 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 consolidated financial statements.

As part of an audit in accordance with Canadian generally accepted auditing standards, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated 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 Company'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 Company'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 consolidated 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 Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance 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 those charged with governance 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.

The engagement partner on the audit resulting in this independent auditor's report is Joseph Man.

RSM Alberta LLP

Edmonton, Alberta
January 28, 2020

Chartered Professional Accountants

RECO INTERNATIONAL GROUP INC.

Consolidated Balance Sheets
September 30, 2019 and 2018
(Expressed in Canadian Dollars)

	<u>2019</u>	<u>2018</u>
ASSETS		
Current Assets		
Cash	\$ 138,730	\$ 135,676
Accounts receivable (Note 4)	918,907	1,150,022
Income taxes receivable	14,586	---
Prepaid expenses and other	<u>37,974</u>	<u>32,569</u>
	1,110,197	1,318,267
Amounts receivable from related parties (Note 5)	---	79,875
Deposits	11,600	11,105
Equipment (Note 6)	<u>158,502</u>	<u>201,785</u>
	<u>\$ 1,280,299</u>	<u>\$ 1,611,032</u>
LIABILITIES		
Current Liabilities		
Accounts payable and accrued liabilities (Note 8)	\$ 372,957	\$ 584,907
Income taxes payable	---	21,345
Amounts payable to related parties (Note 5)	596,630	573,293
Current portion of long-term debt (Note 9)	4,870	7,039
Contract liabilities (Note 17)	<u>94,400</u>	<u>92,071</u>
	1,068,857	1,278,655
Long-term debt (Note 9)	<u>---</u>	<u>4,870</u>
	1,068,857	1,283,525
SHAREHOLDERS' EQUITY		
Share capital (Note 10)	1,105,117	1,105,117
Share-based compensation reserve	208,935	21,665
Deficit	<u>(1,102,610)</u>	<u>(799,275)</u>
	<u>211,442</u>	<u>327,507</u>
	<u>\$ 1,280,299</u>	<u>\$ 1,611,032</u>

Commitments (Note 16)

Approved on behalf of the Board

"Hugh Zhen"

Signed

Director

"Quin Quang Sie"

Signed

Director

See accompanying notes to the consolidated financial statements

RECO INTERNATIONAL GROUP INC.

Consolidated Statements of Operations and Comprehensive Income (Loss)

For the Years Ended September 30, 2019 and 2018

(Expressed in Canadian Dollars)

	2019	2018
Revenue	<u>\$ 2,495,212</u>	<u>\$ 3,685,278</u>
Expenses		
Salaries and benefits	1,109,055	1,270,064
General and administrative	645,343	810,630
Subcontracts	433,301	684,111
Materials and supplies	291,774	512,690
Share-based compensation	187,270	---
Depreciation (Note 6)	<u>44,116</u>	<u>55,613</u>
	<u>2,710,859</u>	<u>3,333,108</u>
Net (loss) income before other items and income taxes	(215,647)	352,170
Other items		
Loss on amounts due from related parties (Note 5)	<u>(22,399)</u>	<u>(40,531)</u>
Net (loss) income before income taxes	(238,046)	311,639
Income taxes expense (recovery) (Note 13)	<u>(14,586)</u>	<u>21,345</u>
Net (loss) income and comprehensive income (loss)	<u>\$ (223,460)</u>	<u>\$ 290,294</u>
Loss per share - basic and diluted (Note 11)	<u>\$ (0.01)</u>	<u>\$ 0.01</u>

See accompanying notes to the consolidated financial statements

RECO INTERNATIONAL GROUP INC.

Consolidated Statements of Changes in Equity
For the Years Ended September 30, 2019 and 2018
(Expressed in Canadian Dollars)

	Share Capital		Share-Based Compensation Reserve	Deficit	Total
	Shares	Amount			
Balance, September 30, 2017	25,635,635	\$ 1,105,117	\$ 21,665	\$(1,089,569)	\$ 37,213
Net income	---	---	---	290,294	290,294
Balance, September 30, 2018	25,635,635	1,105,117	21,665	(799,275)	327,507
Effect of IFRS 9 adoption (Note 5)	---	---	---	(79,875)	(79,875)
Balance, October 1, 2018 as restated	25,635,635	1,105,117	21,665	(879,150)	247,632
Share-based compensation	---	---	187,270	---	187,270
Net loss	---	---	---	(223,460)	(223,460)
Balance, September 30, 2019	<u>25,635,635</u>	<u>\$ 1,105,117</u>	<u>\$ 208,935</u>	<u>\$(1,102,610)</u>	<u>\$ 211,442</u>

See accompanying notes to the consolidated financial statements

RECO INTERNATIONAL GROUP INC.
Consolidated Statements of Cash Flows
For the Years Ended September 30, 2019 and 2018
(Expressed in Canadian Dollars)

	2019	2018
Cash Provided by (Used in):		
Operating Activities		
Net income (loss)	\$ (223,460)	\$ 290,294
Items not involving cash:		
Share-based compensation	187,270	---
Depreciation	44,116	55,613
Interest expenses on long-term debt	---	700
Loss on amount receivable from related parties	22,399	40,531
Net change in non-cash working capital balances (Note 12)	<u>(19,842)</u>	<u>(815,502)</u>
	<u>10,483</u>	<u>(428,364)</u>
Investing Activities		
Deposits	(495)	---
Purchase of equipment	(833)	(1,842)
Advances to related parties	<u>(22,399)</u>	<u>(39,502)</u>
	<u>(23,727)</u>	<u>(41,344)</u>
Financing Activities		
Advances from related parties	220,500	277,237
Repayment to related parties	(197,163)	(155,686)
Repayment of long-term debt	(7,039)	(6,730)
Interest on long-term debt	---	(700)
	<u>16,298</u>	<u>114,121</u>
Increase (decrease) in cash	3,054	(355,587)
Cash, beginning of year	<u>135,676</u>	<u>491,263</u>
Cash, end of year	<u>\$ 138,730</u>	<u>\$ 135,676</u>

See accompanying notes to the consolidated financial statements

RECO INTERNATIONAL GROUP INC.
Notes to the Consolidated Financial Statements
September 30, 2019 and 2018
(Expressed in Canadian Dollars)

1. Reporting Entity

Reco International Group Inc. (the “Company”) was incorporated under the Alberta Business Corporations Act on October 12, 1999 and is in the business of commercial and residential construction and millwork operating in British Columbia. The Company is traded on the TSX Venture Exchange under the symbol RGI.

The head office and principal address of the Company is #100, 2051 Viceroy Place, Richmond, British Columbia, V6V 1Y9.

2. Basis of Presentation

a) Statement of Compliance

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”), being Standards and Interpretations as issued by the International Accounting Standards Board (“IASB”).

The Board of Directors approved these financial statements for issuance on January 28, 2020.

b) Basis of Measurement

These consolidated financial statements have been prepared on the historical cost basis.

c) Functional Currency

These consolidated financial statements are presented in Canadian dollars, which is the Company’s and its subsidiaries’ functional currency.

d) Use of Estimates

The preparation of financial statements in conformity with IFRS requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets and liabilities and the reported amounts of revenues and expenses. Actual results could differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

In preparing these consolidated financial statements, the significant judgements made by management in applying the Company’s accounting policies and the key sources of estimation were valuation of accounts receivable and amounts receivable from related parties, estimated useful life of equipment for use in calculation of depreciation, recognition of deferred tax assets, estimating percentage of completion for revenue recognition, and share-based compensation reserve.

Accounts Receivable and Amounts Receivable from Related Parties

The valuation of accounts receivable and amounts receivable from related parties is based on management’s best estimate of the twelve month or lifetime expected credit loss related to these accounts.

RECO INTERNATIONAL GROUP INC.
Notes to the Consolidated Financial Statements
September 30, 2019 and 2018
(Expressed in Canadian Dollars)

2. **Basis of Presentation** (Continued)

d) Use of Estimates (Continued)

Equipment

The amounts recorded for depreciation is based on management's best estimate of the useful lives of the assets.

Income Taxes

The amounts recorded for deferred income taxes is based on estimates as to the timing of the reversal of temporary differences and tax rates currently substantively enacted. They are also based on the probability of the Company being able to utilize the tax assets.

Revenue

The percentage completion on a project is the basis that management uses to determine the recognition of revenue. The revenue recognized is based on the costs incurred on the project in relation to management's estimate of the total costs expected for the project. However, due to unforeseen changes in the nature or cost of the work to be completed, contract profit can differ significantly from earlier estimates.

Share-based payment reserve

The amounts recorded for share-based compensation reserve is based on the assumptions used in the black-scholes option pricing model. The assumptions for future volatility, market price of the Company's shares, expected lives of the options, expected forfeiture rates, and expected dividends is based on management's best estimate at the time the options are issued.

3. **Summary of Significant Accounting Policies**

The following is a summary of significant accounting policies used in the preparation of these consolidated financial statements:

Principles of Consolidation

The consolidated financial statements consist of Reco International Group Inc. and its wholly owned subsidiaries, Reco Decoration Group Inc. and Z & Z Holdings Ltd. All intercompany balances and transactions have been eliminated on consolidation.

Revenue Recognition

The Company considers their contracts to contain one performance obligation which is satisfied over time. Revenue related to construction projects is recognized by measuring the progress towards the complete satisfaction of the performance obligation using contract costs incurred for work performed relative to the estimated total contract costs. Contract costs include all direct materials, subcontractors' costs and direct labour costs. The Company is acting as the principal in all their arrangements with subcontractors. When consideration is received from customers in advance of the completion of a construction project or the determined stage of completion of a project, the amounts are recorded as contract liability. When it is probable that total contract costs will exceed total contract revenue, the expected loss is recognized immediately as an expense.

RECO INTERNATIONAL GROUP INC.
Notes to the Consolidated Financial Statements
September 30, 2019 and 2018
(Expressed in Canadian Dollars)

3. **Summary of Significant Accounting Policies** (Continued)

Equipment

Equipment is recorded at cost less accumulated depreciation and accumulated impairment losses, if any. Useful lives, residual values and depreciation methods are reviewed and adjusted if appropriate, at the end of each reporting period, with the effect of any changes in estimate being accounted for on a prospective basis. Depreciation is calculated on the declining balance basis at the following annual rates commencing on the date the equipment is available for use:

Equipment	- 20%
Office furniture	- 20%
Computer equipment	- 30%
Vehicles	- 20% - 30%

Income Taxes

Income tax expense consists of current and deferred income taxes. Income tax expense is recognized in profit or loss except to the extent that it relates to items recognized directly in equity, in which case it is recognized in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognized for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognized on the initial recognition of assets or liabilities in a transaction that is not a business combination. In addition, deferred tax is not recognized for taxable temporary differences arising on the initial recognition of goodwill. Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realized simultaneously.

A deferred tax asset is recognized to the extent that it is probable that future taxable profits will be available against which the temporary difference can be utilized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

Earnings Per Share

Earnings per share has been calculated using the weighted average number of common shares outstanding during the period. The Company assumes that common shares are issued for the exercise of options and that the assumed proceeds from the exercise of "in-the-money options" are used to purchase common shares at the average market price during the period. The difference between the number of shares assumed issued and the number of shares assumed purchased is then added to the basic weighted average number of shares outstanding to determine the fully diluted number of common shares outstanding.

RECO INTERNATIONAL GROUP INC.
Notes to the Consolidated Financial Statements
September 30, 2019 and 2018
(Expressed in Canadian Dollars)

3. Summary of Significant Accounting Policies (Continued)

Financial Instruments

Financial assets and financial liabilities are recognized when the Company becomes a party to the contractual provisions of the instrument.

The Company's financial instruments are measured initially at fair value and thereafter based on their classification. The classification depends on the purpose for which the financial instruments were acquired or issued, their characteristics, and the Company's designation of such instruments. At initial recognition financial instruments are classified in the following categories depending on the nature and purpose for which the instruments were acquired:

(i) Financial Assets and Liabilities at Fair Value through Profit or Loss ("FVTPL")

Financial assets and financial liabilities purchased or incurred, respectively, with the intention of generating earnings in the near term are classified as FVTPL. For items classified as FVTPL, the Company initially recognizes such financial assets or liabilities on the consolidated balance sheet at fair value and recognizes subsequent changes in the consolidated statements of operations. Transaction costs incurred are expensed in the consolidated statements of operations. The Company does not have any financial assets or liabilities designated as FVTPL.

(ii) Financial Assets at Fair Value through Other Comprehensive Income (FVTOCI)

Equity investments that are held for trading are classified as FVTPL. For other equity investments, on the day of acquisition the Company can make an irrevocable election to designate them as FVTOCI. Elected investments in equity instruments at FVTOCI are initially recognized at fair value plus transaction costs. Subsequently they are measured at fair value, with gains and losses recognized in other comprehensive income (loss). The Company does not currently hold any assets or liabilities designated as FVTOCI.

(iii) Amortized Cost

The Company classifies financial assets held to collect contractual cash flows at amortized cost, including cash, accounts receivable, deposits and amounts receivable from related parties. The Company initially recognizes the carrying amount of such assets on the consolidated balance sheet at fair value plus directly attributable transaction costs, and subsequently measures these at amortized cost using the effective interest rate method, less any impairment losses.

(iv) Other Financial Liabilities

This category is for financial liabilities that are not classified as FVTPL and includes bank indebtedness, accounts payable and accrued liabilities, amounts payable to related parties, and long-term debt. These financial liabilities are recorded at amortized cost on the consolidated balance sheet.

RECO INTERNATIONAL GROUP INC.
Notes to the Consolidated Financial Statements
September 30, 2019 and 2018
(Expressed in Canadian Dollars)

3. Summary of Significant Accounting Policies (Continued)

Financial Instruments (Continued)

Impairment of Financial Assets

The Company recognizes a loss allowance for expected credit losses on financial assets that are measured at amortized cost as follows:

Cash and due from related parties

The measurement of the loss allowance depends upon the Company's assessment at the end of each reporting period as to whether the financial instrument's credit risk has increased significantly since initial recognition, based on reasonable and supportable information that is available, without undue cost or effort to obtain.

Where there has not been a significant increase in exposure to credit risk since initial recognition, a 12-month expected credit loss allowance is estimated. This represents a portion of the asset's lifetime expected credit losses that is attributable to a default event that is possible within the next 12 months. Where a financial asset has become credit impaired or where it is determined that credit risk has increased significantly, the loss allowance is based on the asset's lifetime expected credit losses. The amount of expected credit loss recognized is measured on the basis of the probability weighted present value of anticipated cash shortfalls over the life of the instrument discounted at the original effective interest rate. A significant increase in credit risk is defined by the Fund as any contractual payment which is more than 30 days past due. Any contractual payment which is more than 90 days past due is considered credit impaired.

Accounts receivable

The Company has applied the simplified approach to measuring expected credit losses, which uses a lifetime expected loss allowance. To measure the expected credit losses, trade receivables have been grouped based on days overdue.

Derecognition

Financial Assets

The Company derecognizes financial assets only when the contractual rights to cash flows from the financial assets expire, or when it transfers the financial assets and substantially all of the associated risks and rewards of ownership to another entity. Gains and losses on derecognition are generally recognized in profit or loss. However, gains and losses on derecognition of financial assets classified as FVTOCI remain within accumulated other comprehensive income (loss).

Financial Liabilities

The Company derecognizes financial liabilities only when its obligations under the financial liabilities are discharged, cancelled or expired. Generally, the difference between the carrying amount of the financial liability derecognized and the consideration paid and payable, including any non-cash assets, is recognized in profit or loss.

RECO INTERNATIONAL GROUP INC.
Notes to the Consolidated Financial Statements
September 30, 2019 and 2018
(Expressed in Canadian Dollars)

3. **Summary of Significant Accounting Policies** (Continued)

Financial Instruments (Continued)

Impairment of Non-financial Assets

Non-financial assets comprising of equipment, are assessed whenever events or changes in circumstances suggest their carrying value may not be recoverable and at the end of each reporting period. Management considers assets to be impaired if the carrying value exceeds the estimated recoverable amount. The recoverable amount is the greater of its value in use and its fair value less costs of disposal. 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 assessment of the time value of money. If impairment is determined to exist, the loss is measured based on the amounts by which the assets carrying values exceed their fair values.

Impairment losses may be reversed, in a subsequent period where the impairment no longer exists or has decreased. The carrying amount after a reversal must not exceed the carrying amount (net of depreciation) that would have been determined had no impairment loss been recognized. A reversal of impairment loss is recognized in profit or loss.

Provisions

A provision is recognized in the balance sheet when the Company has a present legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

Share-based Compensation

The Company uses the Black-Scholes option-pricing model to fair value options granted during the year to directors, officers and employees. The estimated fair value of options on the date of grant is recognized as compensation expense over the vesting period. The number of expected forfeitures is estimated at the grant date and adjustments for actual forfeitures are made as they occur.

RECO INTERNATIONAL GROUP INC.
Notes to the Consolidated Financial Statements
September 30, 2019 and 2018
(Expressed in Canadian Dollars)

3. **Summary of Significant Accounting Policies** (Continued)

Recently Adopted Accounting Pronouncements

IFRS 9, Financial Instruments

IFRS 9 “Financial Instruments” (“IFRS 9”) was issued by the IASB in October 2010 and replaces IAS 39 “Financial Instruments: Recognition and Measurement” (“IAS 39”). IFRS 9 uses a single approach to determine whether a financial asset is measured at amortized cost or fair value, replacing the multiple rules in IAS 39. The approach in IFRS 9 is based on how an entity manages its financial instruments in the context of its business model and the contractual cash flow characteristics of the financial assets. Most of the requirements in IAS 39 for classification and measurement of financial liabilities carried forward unchanged to IFRS 9. The new standard also requires a single impairment method be used, replacing the multiple impairment methods in IAS 39.

The Company adopted IFRS 9 on a retrospective basis. The following table compares the classification of financial instruments under IFRS 9 and IAS 39:

	Original classification under IAS 39	New classification under IFRS 9
Financial assets		
Cash	FVTPL	Amortized cost
Accounts receivable	Loans and receivables	Amortized cost
Deposit	Loans and receivables	Amortized cost
Amounts receivable from related parties	Loans and receivables	Amortized cost
Financial liabilities		
Accounts payable and accrued liabilities	Other financial liabilities	Amortized cost
Amounts payable to related parties	Other financial liabilities	Amortized cost
Long-term debt	Other financial liabilities	Amortized cost

The new standard also includes a new expected credit loss model for calculating impairment on financial assets. This change resulted in an adjustment to the carrying amount for the amounts receivable from related parties at the date of transition, October 1, 2018. See Note 5 for the quantitative impact of the transition adjustment for expected credit loss.

IFRS 9 also introduces new hedge accounting requirements. Since the Corporation does not apply hedge accounting, there was no impact on the financial statements.

RECO INTERNATIONAL GROUP INC.
Notes to the Consolidated Financial Statements
September 30, 2019 and 2018
(Expressed in Canadian Dollars)

3. **Summary of Significant Accounting Policies** (Continued)

Recently Adopted Accounting Pronouncements (Continued)

IFRS 15, Revenue from Contracts with Customers

The Company adopted IFRS 15 using the modified retrospective method. Under the modified retrospective method, the Company will apply the guidance retrospectively only to the most current period presented in the financial statements. To do so, the Company will recognize the cumulative effect of initially applying the standard as an adjustment to the opening balance of retained earnings at the date of initial application, which is October 1, 2018. An entity may elect to apply the modified retrospective method to either all contracts as of the date of initial application or only to contracts that are not completed as of this date. The Corporation has elected to apply the modified retrospective method only to those contracts not completed before the date of initial application. The standard requires revenue to be recognized in a manner that depicts the transfer of promised goods or services to a customer and at an amount that reflects the expected consideration receivable in exchange for the goods or services. This is achieved by applying the following five steps:

1. Identify the contract with a customer;
2. Identify the performance obligations in the contract;
3. Determine the transaction price;
4. Allocate the transaction price to the performance obligations in the contract; and
5. Recognize revenue when the performance obligation is satisfied.

The Company has determined their contracts have one performance obligation that is satisfied over time. Since the Company recognizes revenue by measuring the progress towards complete satisfaction of the performance obligation using costs incurred to date relative to total estimated costs in the current year and prior year, there will be no cumulative effect required to be recognized in opening retained earnings.

Future Accounting Pronouncements

IFRS 16 Leases was issued by the IASB in January 2016. The new standard replaces IAS 17 Leases and requires lessees to recognize all leases on the balance sheet. IFRS 16 removes the classification of leases as either operating leases or finance leases (for the lessee—the lease customer), treating all leases as finance leases. Short-term leases (less than 12 months) and leases of low-value assets are exempt from the requirements. IFRS 16 is effective for the Company's fiscal year beginning October 1, 2019. The Company is currently assessing the impact of this standard on its consolidated financial statements as they expect their premise lease to have an impact from this standard.

4. **Accounts Receivable**

Accounts receivable is comprised of the following items:

	<u>2019</u>	<u>2018</u>
Trade accounts receivable	\$ 916,437	\$ 1,145,950
Goods and Services Tax receivable	<u>2,470</u>	<u>4,072</u>
	<u>\$ 918,907</u>	<u>\$ 1,150,022</u>

RECO INTERNATIONAL GROUP INC.
Notes to the Consolidated Financial Statements
September 30, 2019 and 2018
(Expressed in Canadian Dollars)

5. Related Party Balances and Related Party Transactions

- a) The amounts receivable from related parties are non-interest bearing, unsecured and have no fixed terms of repayment. The related parties are related to the Company by reason of being under common control. During fiscal 2018, the Company recorded a loss of \$40,531 relating to an amount receivable from a company under common control.

On transition to IFRS 9, the Company determined that there was a significant increase in credit risk on amounts due from related parties, as management does not expect to recover any amount on these balances. A life time expected credit loss of \$79,875 (2018 - \$NIL) was recorded for the amounts receivable from related parties through retained earnings under the transitional provision of IFRS 9. The Company also recorded an additional expected credit loss of \$22,399 on an additional funding and an increase of amount due to related parties for the year.

- b) Amounts payable to related parties consist of advances from directors and companies controlled by directors of the Company. Amounts are unsecured, bear no interest and have no specific terms of repayment.
- c) Key management includes senior executives of the Company. The compensation expense paid to key management for employee, consulting and management services are as follows:

	<u>2019</u>	<u>2018</u>
Salaries and other short-term employee benefits	\$ 220,000	\$ 220,000
Management fees	210,000	210,000
Share-based compensation	55,079	---

6. Equipment

	<u>Cost</u>						<u>Balance at September 30, 2019</u>
	<u>Balance at September 30, 2017</u>	<u>Additions</u>	<u>Disposals</u>	<u>Balance at September 30, 2018</u>	<u>Additions</u>	<u>Disposals</u>	
Equipment	\$ 575,118	\$ ---	\$ ---	\$ 575,118	\$ ---	\$ ---	\$ 575,118
Office furniture	85,781	---	---	85,781	---	---	85,781
Computer equipment	68,661	1,842	---	70,503	833	---	71,336
Vehicles	170,973	---	---	170,973	---	---	170,973
	<u>\$ 900,533</u>	<u>\$ 1,842</u>	<u>\$ ---</u>	<u>\$ 902,375</u>	<u>\$ 833</u>	<u>\$ ---</u>	<u>\$ 903,208</u>

	<u>Accumulated Depreciation</u>						<u>Balance at September 30, 2019</u>
	<u>Balance at September 30, 2017</u>	<u>Additions</u>	<u>Disposals</u>	<u>Balance at September 30, 2018</u>	<u>Additions</u>	<u>Disposals</u>	
Equipment	\$ 379,897	\$ 39,045	\$ ---	\$ 418,942	\$ 31,235	\$ ---	\$ 450,177
Office furniture	79,924	1,170	---	81,094	938	---	82,032
Computer equipment	55,913	3,970	---	59,883	3,867	---	63,750
Vehicles	129,243	11,428	---	140,671	8,076	---	148,747
	<u>\$ 644,977</u>	<u>\$ 55,613</u>	<u>\$ ---</u>	<u>\$ 700,590</u>	<u>\$ 44,116</u>	<u>\$ ---</u>	<u>\$ 744,706</u>

RECO INTERNATIONAL GROUP INC.
Notes to the Consolidated Financial Statements
September 30, 2019 and 2018
(Expressed in Canadian Dollars)

6. **Equipment** (Continued)

	Net Book Value	
	Balance at September 30, 2019	Balance at September 30, 2018
Equipment	\$ 124,941	\$ 156,176
Office furniture	3,749	4,687
Computer equipment	7,586	10,620
Vehicles	<u>22,226</u>	<u>30,302</u>
	<u>\$ 158,502</u>	<u>\$ 201,785</u>

7. **Bank Indebtedness**

The Company has available a line of credit of \$100,000 bearing interest at prime plus 3.5%, secured by a general security agreement and is due on demand. \$40,972 has been drawn on the line of credit as at September 30, 2019 (2018 - \$NIL).

8. **Accounts Payable and Accrued Liabilities**

Accounts payable and accrued liabilities are comprised of the following items:

	<u>2019</u>	<u>2018</u>
Trade payables	\$ 230,072	\$ 303,323
Accrued liabilities	113,382	251,812
Goods and Services Tax payable	29,503	26,573
Other payables	<u>---</u>	<u>4,200</u>
	<u>\$ 372,957</u>	<u>\$ 584,907</u>

9. **Long-term Debt**

	<u>2019</u>	<u>2018</u>
Vehicle loan bearing interest of 4.49% per annum, payable in monthly instalments of \$619, including interest, maturing on May 30, 2020, secured by a vehicle with a net book value of \$19,669.	\$ 4,870	\$ 11,909
Current portion	<u>(4,870)</u>	<u>(7,039)</u>
	<u>\$ ---</u>	<u>\$ 4,870</u>

Future minimum payments are as follows:

2020	<u>\$ 4,870</u>
------	-----------------

RECO INTERNATIONAL GROUP INC.
Notes to the Consolidated Financial Statements
September 30, 2019 and 2018
(Expressed in Canadian Dollars)

10. **Share Capital**

Authorized:

- Unlimited common voting shares
- Unlimited redeemable, retractable, non-voting preferred shares

The preferred shares may be issued in one or more series and the directors are authorized to fix the number of shares and determine the designation, rights and privileges attached to each series of shares.

Issued and outstanding:

	<u>Number of Common Shares</u>	<u>Amount</u>
September 30, 2018 and 2019	<u>25,635,635</u>	<u>\$ 1,105,117</u>

Share-Based Compensation Plan

Under the Company's Share-based Compensation Plan, options to purchase common shares of the Company may be granted to directors, officers, key employees and consultants of the Company. These options entitle the holder to purchase one common share at a subscription price that shall not be less than that which may be acceptable to any stock exchange on which the Company's shares are traded. Options expire between two and five years after being issued or ninety days after an employee ceases employment with the Company. The Board of Directors has the discretion to extend the expiration period on cessation of employment. The terms and vesting period of each option is at the discretion of the Board of Directors.

The maximum number of common shares authorized for issuance by the Board of Directors under the plan is limited to 20% of the total issued and outstanding common shares of the Company.

The activity related to stock options is as follows:

	<u>Number of Options</u>	<u>Exercise Price</u>
Balance, October 1, 2018	-	-
Options issued	<u>5,100,000</u>	<u>0.05</u>
Balance, September 30, 2019	<u>5,100,000</u>	<u>\$ 0.05</u>

The Company issued 5,100,000 stock options to purchase common shares of the Company at an exercise price of \$0.05 per common share, expire December 6, 2023 and vests immediately.

RECO INTERNATIONAL GROUP INC.
Notes to the Consolidated Financial Statements
September 30, 2019 and 2018
(Expressed in Canadian Dollars)

10. **Share Capital** (Continued)

The following table summarizes information on stock options outstanding and exercisable at September 30, 2019:

<u>Exercise Price</u>	<u>Number Outstanding</u>	<u>Number Exercisable</u>	<u>Weighted Average Contractual Life (years)</u>
\$ 0.05	5,100,000	5,100,000	4.18

The Company uses the Black-Scholes option-pricing model to estimate the fair value of the stock options. During the period, the Company recorded \$187,270 in share-based compensation expense. The following assumptions were used to estimate the fair value of the stock options granted during the year ended September 30, 2019:

Annualized volatility	158.09%
Risk-free interest rate	2.00%
Expected life of	5 years
Dividend rate	0.00%
Fair value per stock option	\$ 0.037
Share price	\$ 0.04

11. **Loss Per Share**

The basic earnings per share is based on the weighted average number of common shares outstanding as at September 30, 2019 of 25,635,635 (2018 - 25,635,635). The diluted earnings per share is calculated using the weighted average number of common shares of 25,635,635(2018 – 25,635,635) and does not include the stock options which were anti-dilutive.

12. **Non-Cash Working Capital Balances**

The net change in non-cash working capital balances consists of:

	<u>2019</u>	<u>2018</u>
Accounts receivable	\$ 231,115	\$ (376,134)
Income taxes receivable	(14,586)	---
Prepaid expenses	(5,405)	23,359
Accounts payable and accrued liabilities	(211,950)	(144,610)
Income taxes payable	(21,345)	21,345
Deferred revenue	<u>2,329</u>	<u>(339,462)</u>
	<u>\$ (19,842)</u>	<u>\$ (815,502)</u>

RECO INTERNATIONAL GROUP INC.
Notes to the Consolidated Financial Statements
September 30, 2019 and 2018
(Expressed in Canadian Dollars)

13. **Income Taxes**

The income tax provision reported differs from the amount computed by applying the combined Canadian federal and provincial rate to income (loss) before income taxes. The reasons for the difference and the related tax effects are as follows:

	<u>2019</u>	<u>2018</u>
Income (loss) before income taxes	\$ (238,046)	\$ 311,639
Expected rate	<u>26.79%</u>	<u>26.75%</u>
Expected tax expense (recovery)	(63,770)	83,363
Tax effected adjustments:		
Expenses not deductible for tax	59,035	16,759
Temporary difference for tax purposes	(827)	(1,207)
Net effect of non-capital losses	<u>(9,024)</u>	<u>77,570</u>
Non-capital losses not recognized	<u>\$ (14,586)</u>	<u>\$ 21,345</u>

The consolidated financial statements do not reflect potential tax reductions available through the application of losses carried forward against future years' earnings otherwise subject to income taxes. These losses amounting to \$590,318 may be carried forward and expire as follows:

2028	\$ 16,253
2029	---
2030	---
2031	---
2032	95,615
2033	88,307
2034	73,743
2035	93,710
2036	61,475
2037	88,999
2038	---
2039	72,216
	<u>\$ 590,318</u>

The Company has not recognized deferred tax assets for which it is not probable that realization will occur. Significant components of the Company's deferred tax assets are as follows:

	<u>2019</u>	<u>2018</u>
Deferred Tax Assets		
Excess of tax value over book value of assets	\$ (914)	\$ (927)
Tax basis of cumulative eligible capital	9,900	12,381
Loss carry forwards	<u>138,012</u>	<u>153,197</u>
	146,998	164,651
Unrecognized deferred tax asset	<u>(146,998)</u>	<u>(164,651)</u>
Net deferred income tax asset	<u>\$ ---</u>	<u>\$ ---</u>

RECO INTERNATIONAL GROUP INC.
Notes to the Consolidated Financial Statements
September 30, 2019 and 2018
(Expressed in Canadian Dollars)

14. Financial Instruments

The Company's financial instruments consist of cash, accounts receivable, amounts receivable from related parties, deposits, accounts payable and accrued liabilities, amounts payable to related parties and long-term debt.

Financial risk management

The Company's activities are exposed to a variety of financial risks: interest rate risk, credit risk and liquidity risk. The Company's overall risk management program focuses on the unpredictability of financial and economic markets and seeks to minimize potential adverse effects on the Company's financial results. Risk management is carried out by financial management in conjunction with overall corporate governance.

Interest rate risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate due to changes in market interest rates. The Company is exposed to interest rate fair value risk arising from its fixed rate long-term debt. Management does not believe this risk is significant.

Credit risk

The Company's exposure to credit risk relates to cash, deposits and accounts receivable that arises from the possibility that the third party does not satisfy its contractual obligations. The credit risk for cash is mitigated with the Company holding cash with major financial institutions. The credit risk for deposits is low due to the credit worthiness of the counter-party. The Company minimizes its exposure to credit risk on accounts receivable through a program of credit evaluation of customers or obtaining deposits on projects. The Company performs continuous evaluation of its accounts receivable and records an expected credit loss based on recoverability of receivable balances from each customer taking into account historic collection of past due accounts. As at September 30, 2019, the Company has \$165,431 (2018 - \$98,237) of accounts receivable that are past due (over 90 days). There has been no expected credit loss recorded for accounts receivable since the amount was determined to be nominal based on historical collections. As at September 30, 2019, approximately 74% (2018 - 88%) of contract revenue receivable are from three customers (2018 – three customers).

Trade accounts receivable aging details:

	<u>2018</u>	<u>2017</u>
Current	\$ 429,762	\$ 83
0 - 90 days	321,244	1,047,630
Over 90 days	<u>165,431</u>	<u>98,237</u>
	<u>\$ 916,437</u>	<u>\$ 1,145,950</u>

Liquidity risk

The Company's exposure to liquidity risk is dependent on the collection of accounts receivable, purchasing commitments and obligations or raising of funds to meet commitments and sustain operations. The Company controls liquidity risk by management of working capital and cash flows. As at September 30, 2019, the Company was holding cash of \$138,730 (2018 - \$135,676), trade accounts receivable of \$916,437 (2018 - \$1,145,950) and had a working capital surplus of \$41,340 (2018 - surplus of \$39,612). The contractual maturity of the Company's liabilities of \$377,827 (2018 - \$591,947) will be paid within one year and the amounts payable to related parties of \$596,630 (2018 - \$573,293) have no terms of repayment.

RECO INTERNATIONAL GROUP INC.
Notes to the Consolidated Financial Statements
September 30, 2019 and 2018
(Expressed in Canadian Dollars)

14. **Financial Instruments** (Continued)

Fair value

The fair value of cash, accounts receivables, deposits, accounts payable and accrued liabilities and amounts payable to related parties approximate its carrying amount due to the short-term nature of the financial instrument. The fair value of the long-term debt approximates its carrying amount since its term approximates market terms.

The following provides an analysis of financial instruments that are measured at fair value, grouped into levels 1 to 3 based on the degree to which the fair value is observable:

- Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2 fair value measurements are those derived from inputs other than quoted prices included within level 1 that are not observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data.

As at September 30, 2019 and 2018, the Company does not have any financial instruments measured at fair value.

15. **Capital Management**

The Company's objective when managing capital is to maintain adequate cash resources to support planned activities which include sustaining continuing operations. The Company includes shareholders' equity of \$211,442 (2018 – shareholders' equity of \$327,507) and amounts payable to related parties of \$596,630 (2018 - \$573,293) in the definition of capital.

In managing capital, the Company estimates its future cash requirements by preparing a budget. The budget establishes the activities for the upcoming year and estimates the costs associated with these activities.

Historically, funding for the Company's plan was primarily managed through the issuance of additional common shares, through its commercial activities and through obtaining financing. There are no assurances that funds will be made available to the Company when required. The Company is not subject to externally imposed capital requirements.

RECO INTERNATIONAL GROUP INC.
Notes to the Consolidated Financial Statements
September 30, 2019 and 2018
(Expressed in Canadian Dollars)

16. Commitments

- a) The Company has a lease agreement for its present location which expires May 31, 2022. The remaining commitment on the lease excluding operating costs is as follows:

2020	109,267
2021	111,750
2022	<u>74,500</u>
Total	<u>\$ 295,517</u>

- b) The Company has signed consulting and management contracts with companies that are controlled by directors of the Company to provide services from October 1, 2019 to September 30, 2020 for \$210,000 per annum.

17. Contract Liabilities

The Company has two construction contracts (2018 – two construction contracts) in progress and the following is financial information for these contracts in progress:

	<u>2019</u>	<u>2018</u>
Contract liabilities recognized in revenue	\$ 92,071	\$ 431,533
Contract liabilities	\$ 94,400	\$ 92,071