

BQE Water

BQE WATER INC.

Condensed Consolidated Interim Financial Statements (Unaudited)

For the three and nine months ended September 30, 2018 and 2017

NOTICE TO READER

The accompanying condensed consolidated interim financial statements of the Company have been prepared by and are the responsibility of the Company's management. The Company's independent auditor has not performed a review of these condensed consolidated interim financial statements in accordance with standards established by the Canadian Institute of Chartered Accountants for a review of interim financial statements by an entity's auditor.

BQE WATER INC.Condensed Consolidated Interim Statements of Financial Position
(Unaudited)

| | | September 30 2018 \$ | December 31 2017 \$ |
|---|--------|----------------------------|---------------------------|
| | note | | |
| Assets | | | |
| Current assets | | | |
| Cash | | 88,609 | 984,298 |
| Trade and other receivables | 5 | 2,212,107 | 680,530 |
| Prepaid and other deposits | | 39,842 | 42,956 |
| Total current assets | | 2,340,558 | 1,707,784 |
| Non-current assets | | | |
| Plant and equipment | 7 | 50,573 | 42,463 |
| Investment in joint ventures | 8 | 6,074,948 | 5,095,256 |
| Deposits | | 34,699 | 20,386 |
| Total non-current assets | | 6,160,220 | 5,158,105 |
| Total assets | | 8,500,778 | 6,865,889 |
| Liabilities | | | |
| Current liabilities | | | |
| Loans | 11 | 1,822,625 | - |
| Trade payable and accrued liabilities | 6, 9 | 1,709,993 | 783,799 |
| Deferred revenues | | 123,641 | 29,198 |
| Deferred benefits | 10 | 105,527 | 159,835 |
| Total current liabilities | | 3,761,786 | 972,832 |
| Non-current liabilities | | | |
| Convertible loan | 11 | - | 1,497,726 |
| Total liabilities | | 3,761,786 | 2,470,558 |
| Shareholders' Equity | | | |
| Share capital | 10, 12 | 54,719,814 | 54,719,814 |
| Contributed surplus | 12 | 10,152,200 | 10,058,149 |
| Equity component of convertible loan | 11 | 86,575 | 86,575 |
| Accumulated other comprehensive income | | 1,243,369 | 1,398,709 |
| Accumulated deficit | | (61,462,966) | (61,867,916) |
| Total shareholders' equity | | 4,738,992 | 4,395,331 |
| Total liabilities and shareholders' equity | | 8,500,778 | 6,865,889 |
| Going concern (note 2(b)) | | | |
| Commitments (note 15) | | | |

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

BQE WATER INC.

Condensed Consolidated Interim Statements of Income and Other Comprehensive Loss
For the three and nine months ended September 30, 2018 and 2017
(Unaudited)

| | note | 3 months ended September 30 | | 9 months ended September 30 | |
|---|------|-----------------------------|------------|-----------------------------|-------------|
| | | 2018 | 2017 | 2018 | 2017 |
| | | \$ | \$ | \$ | \$ |
| Revenue | | 1,893,177 | 1,578,327 | 2,960,418 | 3,199,204 |
| Operating costs (excluding depreciation) | | 573,098 | 641,556 | 1,471,836 | 1,715,690 |
| Operating margin before depreciation | | 1,320,079 | 936,771 | 1,488,582 | 1,483,514 |
| General and administration | | 368,638 | 383,120 | 1,081,983 | 1,254,484 |
| Sales and development | | 211,319 | 263,115 | 863,685 | 854,636 |
| Stock-based compensation | 10 | 36,923 | 34,476 | 101,031 | 43,082 |
| Depreciation of plant and equipment | 7 | 4,122 | 31,472 | 11,886 | 97,689 |
| Share of results of equity accounted joint ventures | 8 | (301,785) | (469,792) | (1,095,641) | (1,267,958) |
| Income from operations and joint ventures | | 1,000,862 | 694,380 | 525,638 | 501,581 |
| Finance costs, net | | (38,404) | (55,425) | (102,310) | (159,306) |
| Foreign exchange loss | | (18,653) | (23,074) | (18,378) | (37,561) |
| Other income | | - | 60,978 | - | 62,978 |
| Income before income taxes | | 943,805 | 676,859 | 404,950 | 367,692 |
| Income tax recovery | | - | 152,740 | - | 152,740 |
| Net income for the period | | 943,805 | 829,599 | 404,950 | 520,432 |
| Other comprehensive loss | | | | | |
| <i>Items that will be reclassified subsequently to loss</i> | | | | | |
| Translation loss on foreign operations | | (318,427) | (97,467) | (155,340) | (139,970) |
| Comprehensive income for the period | | 625,378 | 732,132 | 249,610 | 380,462 |
| Net income per share | | | | | |
| Basic and diluted | | 0.01 | 0.01 | 0.00 | 0.01 |
| Weighted average number of shares outstanding | | | | | |
| Basic and diluted | | 93,966,672 | 93,966,672 | 93,966,672 | 93,966,672 |

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

BQE WATER INC.

Condensed Consolidated Interim Statements of Changes in Equity
 For the nine months ended September 30, 2018 and 2017
 (Unaudited)

| | | Number of Shares | 9 months ended Sept. 30, 2018 \$ | Number of Shares | 9 months ended Sept. 30, 2017 \$ |
|---|------|---------------------|--|---------------------|--|
| | note | | | | |
| Share Capital | | | | | |
| Balance, beginning of the period | 12 | 93,966,672 | 54,719,814 | 93,966,672 | 54,719,814 |
| | | | - | | - |
| Balance, end of the period | | 93,966,672 | 54,719,814 | 93,966,672 | 54,719,814 |
| Contributed surplus | | | | | |
| Balance, beginning of the period | | | 10,058,149 | | 10,047,271 |
| Share-based payments | 10 | | 94,051 | | 2,610 |
| Balance, end of the period | | | 10,152,200 | | 10,049,881 |
| Equity component of convertible loan | | | | | |
| Balance, beginning of the period | | | 86,575 | | 84,614 |
| Issuance of convertible loan | 11 | | - | | 1,961 |
| Balance, end of the period | | | 86,575 | | 86,575 |
| Accumulated other comprehensive income | | | | | |
| Balance, beginning of the period | | | 1,398,709 | | 1,410,982 |
| Other comprehensive loss for the period | | | (155,340) | | (139,970) |
| Balance, end of the period | | | 1,243,369 | | 1,271,012 |
| Accumulated deficit | | | | | |
| Balance, beginning of the period | | | (61,867,916) | | (61,506,865) |
| Net income for the period | | | 404,950 | | 520,432 |
| Balance, end of the period | | | (61,462,966) | | (60,986,433) |
| Total shareholders' equity | | | | | |
| Balance, beginning of the period | | | 4,395,331 | | 4,755,816 |
| Share-based payments | 10 | | 94,051 | | 2,610 |
| Issuance of convertible loan | 11 | | - | | 1,961 |
| Net income for the period | | | 404,950 | | 520,432 |
| Other comprehensive loss for the period | | | (155,340) | | (139,970) |
| Balance, end of the period | | | 4,738,992 | | 5,140,849 |

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

BQE WATER INC.

Condensed Consolidated Interim Statements of Cash Flows
For the nine months ended September 30, 2018 and 2017
(Unaudited)

| | | 9 months ended September 30 | |
|---|------|------------------------------------|-------------|
| | | 2018 | 2017 |
| | | \$ | \$ |
| | note | | |
| Operating activities | | | |
| Net income for the period | | 404,950 | 520,432 |
| Items not affecting cash | | | |
| Income tax recovery | | - | (152,740) |
| Bad debt recovery | | - | (60,978) |
| Share of results of equity accounted joint ventures | 8 | (1,095,641) | (1,267,958) |
| Interest expense | | 102,310 | 159,306 |
| Gain on disposal of equipment | | - | (2,000) |
| Depreciation of plant and equipment | 7 | 11,886 | 97,689 |
| Amortization of deferred lease inducement | | - | (23,083) |
| Net foreign exchange loss | | 2,239 | 36,023 |
| Stock-based compensation | 10 | 101,031 | 43,082 |
| | | (473,225) | (650,227) |
| Change in non-cash working capital items | 14 | (602,449) | (118,857) |
| Cash used in operations | | (1,075,674) | (769,084) |
| Income taxes paid | | - | - |
| Net cash used in operating activities | | (1,075,674) | (769,084) |
| Investing activities | | | |
| Purchase of equipment | 7 | (19,996) | (35,592) |
| Proceeds from disposal of equipment | | - | 2,000 |
| Contributions made to joint ventures | 8 | (70,500) | (85,815) |
| Interest received | | 4,514 | 6,619 |
| Net cash used in investing activities | | (85,982) | (116,740) |
| Financing activities | | | |
| Proceeds from loans | 11 | 325,930 | 19,666 |
| Interest paid | 11 | (73,417) | (117,552) |
| Net cash received (used) in financing activities | | 252,513 | (97,886) |
| Effect of exchange rate changes on cash | | 13,454 | (22,338) |
| Change in cash | | (895,689) | (1,006,048) |
| Cash, beginning of the period | | 984,298 | 2,231,798 |
| Cash, end of the period | | 88,609 | 1,225,750 |

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

BQE WATER INC.

Notes to Condensed Consolidated Interim Financial Statements
For the three and nine months ended September 30, 2018
(Unaudited)

1. DESCRIPTION OF BUSINESS AND NATURE OF OPERATIONS

BQE Water Inc. is the ultimate parent company of its consolidated group ("the "Company"). The Company is an integrated water services provider with unique expertise and intellectual property related to the management and treatment of water at mines and metallurgical facilities focused on reducing life cycle costs and eliminating long-term liabilities.

The Company is a publicly listed company incorporated and domiciled in Canada with limited liability under the legislation of the Province of British Columbia. The Company's shares are listed on the TSX Venture Exchange trading under the symbol BQE. The address of its registered office is Suite 250 – 900 Howe Street, Vancouver, British Columbia, V6Z 2M4, Canada.

2. BASIS OF PREPARATION

a. Statement of compliance

These condensed consolidated interim financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"), and interpretations of the IFRS Interpretations Committee ("IFRIC"), effective as of September 30, 2018.

The Company's Board of Directors approved these condensed consolidated interim financial statements on November 20, 2018.

b. Going concern assumption

The condensed consolidated interim financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the settlement of liabilities in the normal course of business.

For the nine months ended September 30, 2018, the Company incurred a net income of \$404,950 (\$520,432 in 2017) and used net cash in operating activities of \$1,075,674 (\$769,084 in 2017). At September 30, 2018, the Company had a working capital deficit of \$1,421,228 (positive working capital of \$734,952 at December 31, 2017) and a cumulative deficit of \$61,462,966 (\$61,867,916 at December 31, 2017).

Management and the Board of Directors of the Company successfully replaced the original \$1.5 million convertible loan due January 6, 2018 with replacement loan due January 6, 2019. Also, during Q2 of 2018, Management and the Board of Directors successfully signed short-term loans contracts with employees of the Company and the Company's joint venture partner in China. The extension of the convertible loan and the newly established short-term loans will ensure that the Company has sufficient levels of working capital for the rest of 2018. The Company expects to generate sufficient working capital to enable us to repay the principle amount of the short-term loans and have sufficient cash reserves to meet ongoing operating requirements over the next 12 months. This also assumes that the Company is able to continue successful operations at its Raglan and Chinese joint venture plants, market prices for metals and foreign exchange rates remain at current levels, the Company maintains or further decreases operating expenses, successfully repatriates funds from its Chinese joint venture, and secures and completes new sales contracts. Beyond this point, the Company will need to secure new sources of working capital to continue operations.

Historically, the Company has not yet realized profitable operations and has relied on non-operational sources of financing to fund its operations. Whether and when the Company can attain profitability and positive cash flows is uncertain. While the Company has been successful in securing financing in the past, there is uncertainty whether financing will be available in the future on terms acceptable to the Company. Accordingly, there is a material uncertainty that may cast significant doubt upon the Company's ability to continue as a going concern. These consolidated financial statements do not include adjustments to the recoverability and classification on recorded assets and liabilities and related expenses that might be necessary should the Company be unable to continue as a going concern. If the going concern assumption is not appropriate, material adjustments to the financial statements could be required.

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Notes to Condensed Consolidated Interim Financial Statements
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c. Basis of measurement

These condensed consolidated interim financial statements have been prepared under the historical cost basis except for deferred share units and restricted share units, which are measured at fair value through profit or loss.

d. Basis of consolidation

These condensed consolidated interim financial statements incorporate the financial statements of the Company, and the entities controlled by the Company, and the share of net assets and net earnings or losses in entities which the Company is a joint venture partner. The principal subsidiaries of the Company, which are accounted for under the consolidation method, are as follows:

| Entity | Country of incorporation and operation | Ownership interest as at Sept. 30, 2018 | Ownership interest as at Dec. 31, 2017 |
|---|--|---|--|
| Biomet Mining Corporation | Canada | 100% | 100% |
| BioteQ Water (Chile) SpA | Chile | 100% | 100% |
| BioteQ Water Mexico S.A. de C.V. | Mexico | 100% | 100% |
| BioteQ (Shanghai) Water Treatment Technologies Co. Ltd. | China | 100% | 100% |

The joint ventures of the Company, which are accounted for under the equity method, are as follows:

| Entity | Country of incorporation and operation | Ownership interest as at Sept. 30, 2018 | Ownership interest as at Dec. 31, 2017 |
|---|--|---|--|
| JCC-BioteQ Environmental Technologies Co. Ltd. | China | 50% | 50% |
| Shandong MWT BioteQ Environmental Technologies Co. Ltd. | China | 20% | 20% |

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies as set out below have been consistently applied to all periods presented in these condensed consolidated interim financial statements and are prepared using the same accounting policies and methods of computation as the annual audited consolidated financial statements of the Company for the year ended December 31, 2017, with the exception of the adoption of IFRS 15 and IFRS 9 as described below. Certain prior year comparative figures have been reclassified to comply with the current year's presentation.

IFRS 15 – Revenue from Contracts with Customers

The Company adopted IFRS 15, *Revenue from Contracts with Customers* ("IFRS 15") retrospectively on January 1, 2018. IFRS 15 supersedes IAS 11, *Construction Contracts* and IAS 18, *Revenue*, and related interpretations. The Company has detailed below the impact of the transition to IFRS 15 on its accounting policy for revenue recognition.

The Company applied IFRS 15 retrospectively to all contracts that were not completed by January 1, 2018, the date of initial application, in order to determine if a restatement was required for prior periods presented. The Company performed a comprehensive review of existing contracts, control processes and revenue recognition methodology. In evaluating the impact of IFRS 15 on previously reported comparative figures, the Company determined that there was no change required as the existing revenue recognition practices met the requirements of IFRS 15.

Revenue is recognized by applying the five-step model under IFRS 15. The standard requires entities to recognize revenue when the control of the goods or services passes to the customer. For the Company's revenue earned from the operation and maintenance of water treatment plants, the Company concluded there were no changes to the classification and timing of revenue recognition under the new standard as the point of transfer of risk and reward for goods and services and transfer of control occur at the same time. In addition, the standard requires entities to apportion revenue earned from contracts to

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Notes to Condensed Consolidated Interim Financial Statements
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individual performance obligations, on a relative standalone selling price basis. The Company also earns revenue from technical services relating to water management, including engineering, laboratory and pilot demonstrations. For technical services contracts, the Company may defer and recognize the revenue over time as each obligation within the contracts are fulfilled. Given that the majority of our technical services contracts have the clause that allow the Company to have an enforceable right to payment for performance completed to date, the Company concluded there were no changes to the classification and timing of revenue recognition as the Company will continue to recognize revenue over time using project stage of completion based on costs incurred and labour hours expended.

IFRS 15 requires that variable consideration should only be recognized to the extent that it is highly probable that a significant reversal in the amount of cumulative revenue recognized will not occur. Recognition requirements surrounding contract modifications have been implemented, where the Company is required to provide stronger evidence of customer acceptance and completion of modified performance obligations. For any change in transaction price as a result of contract modifications, the Company will only recognize revenue to the extent that it is highly probable that the revenue will not reverse in the future.

IFRS 9 – Financial Instruments

On July 24, 2014, the IASB issued the final version of IFRS 9, *Financial Instruments* (“IFRS 9”) to replace IAS 39, *Financial Instruments: Recognition and Measurement*. The Company adopted IFRS 9 retrospectively on January 1, 2018. The adoption of this standard did not have a material impact on the condensed consolidated interim financial statements. IFRS 9 introduces new requirements for the classification and measurement of financial assets. Under IFRS 9, financial assets are classified and measured based on the business model in which they are held and the characteristics of their contractual cash flows. The standard introduces additional changes relating to financial liabilities and amends the impairment model by introducing a new “expected credit loss” model for calculating impairment. It also includes a new general hedge accounting standard which aligns hedge accounting more closely with risk management. The Company’s policies and procedures surrounding the identification of credit risk and the recognition of credit losses comply with the requirements of this standard.

4. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

The preparation of the Company’s condensed consolidated interim financial statements in conformity with IFRS requires the Company’s management to make judgments, estimates and assumptions about future events that affect the amounts reported in the condensed consolidated interim financial statements and related notes to the financial statements. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

Estimates and assumptions are continually evaluated and are based on management’s experience and other facts and circumstances. Revisions to estimates and the resulting effects on the carrying amounts of the Company’s assets and liabilities are accounted for prospectively. The judgments, estimates and assumptions applied in these condensed consolidated interim financial statements, including key sources of estimation uncertainty were the same as those applied in the Company’s last annual audited consolidated financial statements for the year ended December 31, 2017, other than those additional areas which have arisen as a result of the implementation effective January 1, 2018 of IFRS 15 as discussed earlier.

BQE WATER INC.

Notes to Condensed Consolidated Interim Financial Statements
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 (Unaudited)

5. TRADE AND OTHER RECEIVABLES

| | Sept. 30, 2018 | Dec. 31, 2017 |
|-----------------------------|------------------|----------------|
| | \$ | \$ |
| Trade receivables | 2,124,000 | 322,198 |
| Unbilled receivables | 86,387 | 246,495 |
| Value added tax receivables | - | 12,467 |
| Other | 1,720 | 99,370 |
| | <u>2,212,107</u> | <u>680,530</u> |

6. RELATED PARTY TRANSACTIONS

The following transactions were carried out with related parties of the Company:

- a) For the three and nine months ended September 30, 2018 and 2017, the compensation awarded to the Company's key management, which includes the Board of Directors and executive management, are as follows:

| | 3 months ended Sept. 30 | | 9 months ended Sept. 30 | |
|--|-------------------------|----------------|-------------------------|----------------|
| | 2018 | 2017 | 2018 | 2017 |
| | \$ | \$ | \$ | \$ |
| Salaries, fees and short-term benefits | 139,454 | 172,128 | 309,076 | 442,519 |
| Share-based payments | 13,961 | - | 40,685 | 2,610 |
| | <u>153,415</u> | <u>172,128</u> | <u>349,761</u> | <u>445,129</u> |

Included in the trade payables and accrued liabilities as of September 30, 2018 is \$147,379 (\$12,231 at December 31, 2017) of management consulting service fees with companies owned by the Company's management, director fees and termination benefits.

- b) The Company has multiple loan agreements with multiple related parties. These lenders include the Company's joint venture, certain directors, shareholders, management and employees of the Company. Details of the loans with various related parties are described in note 11.
- c) Included in the trade payables and accrued liabilities as of September 30, 2018 is \$96,400 (\$96,400 at December 31, 2017) of contribution of registered capital payable to the Company's joint venture as described in note 8(b).

BQE WATER INC.

Notes to Condensed Consolidated Interim Financial Statements
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(Unaudited)

7. PLANT AND EQUIPMENT

| | Pilot plants \$ | Other ¹ \$ | Total \$ |
|-------------------------------|--------------------|--------------------------|---------------|
| As at Dec. 31, 2017 | | | |
| Opening net book value | 199,882 | 17,128 | 217,010 |
| Additions | - | 39,545 | 39,545 |
| Depreciation | (199,882) | (14,210) | (214,092) |
| Closing net book value | - | 42,463 | 42,463 |
| As at Dec. 31, 2017 | | | |
| Cost | 580,593 | 568,065 | 1,148,658 |
| Accumulated depreciation | (580,593) | (525,602) | (1,106,195) |
| Closing net book value | - | 42,463 | 42,463 |
| As at Sept. 30, 2018 | | | |
| Opening net book value | - | 42,463 | 42,463 |
| Additions | - | 19,996 | 19,996 |
| Depreciation | - | (11,886) | (11,886) |
| Closing net book value | - | 50,573 | 50,573 |
| As at Sept. 30, 2018 | | | |
| Cost | 580,593 | 588,062 | 1,167,816 |
| Accumulated depreciation | (580,593) | (537,489) | (1,117,243) |
| Closing net book value | - | 50,573 | 50,573 |

¹Other comprises of leasehold improvements, office and lab equipment and computer equipment.

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Notes to Condensed Consolidated Interim Financial Statements
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(Unaudited)

8. INVESTMENT IN JOINT VENTURES

Investment in joint ventures is comprised of:

| | JCC-BQE \$ | MWT-BQE \$ |
|--|---------------|---------------|
| Balance, January 1, 2017 | 4,231,567 | - |
| Share of net income (loss) | 1,170,739 | (21,422) |
| Share of translation loss on foreign operation | (5,942) | (65) |
| Contributions made | 148,379 | 96,400 |
| Distributions received | (524,400) | - |
| Balance, December 31, 2017 | 5,020,343 | 74,913 |
| Share of net income (loss) | 1,124,387 | (28,746) |
| Share of translation gain on foreign operation | (178,155) | (8,294) |
| Contributions made | 70,500 | - |
| Balance, September 30, 2018 | 6,037,075 | 37,873 |

a. JCC-BioteQ Environmental Technologies Co. Ltd.

During 2006, the Company signed a definitive joint venture agreement with Jiangxi Copper Corporation ("JCC") for the operation of a water treatment facility located at JCC's Dexing Mine in Jiangxi Province, China. The joint venture, which forms a 50/50 share joint venture company between the Company and JCC, is called JCC-BioteQ Environmental Technologies Co. Ltd ("JCC-BQE"). The joint venture builds and operates water treatment plants using the Company's technologies. The agreement includes a license contract whereby the Company will provide its patented technology on a royalty-free basis to the joint venture company for use at Dexing Mine and also five potential additional sites owned and operated by JCC.

The joint venture sells all of the metal concentrate recovered in its operations to the joint venture partner, JCC. All related party sales are recorded on the date of sale at the fair market price of the metal with adjustments in accordance with the agreed terms. Currently, the joint venture operates three water treatment plants.

Any cash distributions from the joint venture to the Company must be unanimously approved by both partners and comply with Chinese tax and regulatory requirements. Distributions are also subject to Chinese withholding taxes and minimum capital requirements as applicable. Currently, the Company and JCC have a standing agreement to distribute excess cash reserves annually. The partners will take into consideration factors such as operating performance of the plants, future capital requirements and working capital flexibility in determining the cash amount to be distributed in a given year.

The joint venture derives its revenue from recovered copper sales, which is subject to risks that are beyond the control of the joint venture. The copper recovery rate is dependent on the rainfall in the region and the grade of copper in the water treated, while the revenue is exposed to the world commodity price risk.

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Notes to Condensed Consolidated Interim Financial Statements
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(Unaudited)

The financial statements of the Company's 50% interest in the JCC-BQE joint venture is presented as follows:

Statement of financial position

| | Sept. 30, 2018 | Dec. 31, 2017 |
|--|------------------|------------------|
| | \$ | \$ |
| Assets | | |
| Current assets | | |
| Cash | 3,067,793 | 1,562,058 |
| Short-term investments | 113,040 | - |
| Trade and other receivables | 113,285 | 28,178 |
| Income taxes recoverable | - | 58,940 |
| Inventory | 36,716 | 33,663 |
| Prepaid expenses | 12,901 | 977 |
| | <u>3,343,735</u> | <u>1,683,816</u> |
| Non-current assets | | |
| Plant and equipment | 3,609,151 | 4,029,345 |
| Deferred tax assets | 63,764 | 65,254 |
| | <u>3,672,915</u> | <u>4,094,599</u> |
| Total assets | <u>7,016,650</u> | <u>5,778,415</u> |
| Liabilities | | |
| Current liabilities | | |
| Accounts payable and accrued liabilities | 883,518 | 758,072 |
| Income taxes payable | 96,057 | - |
| | <u>979,575</u> | <u>758,072</u> |
| Total liabilities | <u>979,575</u> | <u>758,072</u> |
| Partner's Equity | | |
| Joint venture partner equity | 3,802,903 | 3,732,403 |
| Accumulated other comprehensive income | 1,265,811 | 1,443,966 |
| Retained earnings (deficit) | 968,361 | (156,026) |
| Total partner's equity | <u>6,037,075</u> | <u>5,020,343</u> |
| Total liabilities and partner's equity | <u>7,016,650</u> | <u>5,778,415</u> |

BQE WATER INC.

Notes to Condensed Consolidated Interim Financial Statements
 For the three and nine months ended September 30, 2018
 (Unaudited)

Statements of operations and comprehensive income

| | 3 months ended Sept. 30 | | 9 months ended Sept. 30 | |
|--|-------------------------|-----------|-------------------------|-----------|
| | 2018 | 2017 | 2018 | 2017 |
| | \$ | \$ | \$ | \$ |
| Revenue | 1,594,856 | 1,568,649 | 4,641,345 | 4,238,052 |
| Plant operating costs (excluding depreciation) | 1,039,926 | 810,916 | 2,651,975 | 2,124,191 |
| | 554,930 | 757,733 | 1,989,370 | 2,113,861 |
| General and administration | 14,408 | 44,896 | 223,325 | 240,584 |
| Depreciation of plant and equipment | 115,109 | 124,814 | 369,737 | 382,209 |
| Income from operations | 425,413 | 588,023 | 1,396,308 | 1,491,068 |
| Finance income | 8,479 | 1,097 | 10,052 | 1,699 |
| Other income, net | 1,296 | 23,492 | 46 | 23,054 |
| Income before income taxes | 435,188 | 612,612 | 1,406,406 | 1,515,821 |
| Current income tax expense | (123,169) | (142,820) | (282,019) | (341,859) |
| Deferred tax recovery | - | - | - | 93,996 |
| Net income for the period | 312,019 | 469,792 | 1,124,387 | 1,267,958 |
| Other comprehensive loss | | | | |
| Translation loss on foreign operation | (324,371) | (100,478) | (178,155) | (154,429) |
| Comprehensive (loss) income for the period | (12,352) | 369,314 | 946,232 | 1,113,529 |

b. Shandong MWT BioteQ Environmental Technologies Co. Ltd.

During 2016, the Company signed a joint venture agreement with Beijing MWT Water Treatment Project Limited Company (“MWT”) for the construction and operation of a water treatment plant located in Shandong Province of China. The joint venture between the Company and MWT is called Shandong MWT BioteQ Environmental Technologies Co., Ltd. (“MWT-BQE”). The joint venture will build a water treatment plant located on a vacant lot owned by Shandong Zhaojin Group Zhaoyuan Gold Smelting Co., Ltd (“Zhaoye”). The joint venture will then operate the plant using the Company’s patented technology to recover and sell copper and zinc metals from Zhaoye’s industrial waste water stream in order to make profits.

The Company is entitled to 20% of the after-tax profits of the joint venture. Upon establishment of MWT-BQE, the Company is required to pay a cash contribution as registered capital of \$96,400 (RMB \$500,000), which is 4.35% of the total registered capital of the joint venture. The joint venture have completed the construction of the water treatment plant and has fully commissioned the plant to be operational during Q3 2018.

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The sections of the statement of financial position of the Company's portion of interest in the MWT-BQE joint venture is presented as follows:

| | Sept. 30, 2018 | Dec. 31, 2017 |
|---------------------|----------------|---------------|
| | \$ | \$ |
| Current assets | 13,802 | 78,429 |
| Plant and equipment | 80,036 | 19,297 |
| Current liabilities | 10,119 | 5,951 |
| Partner's equity | 37,921 | 74,961 |

The statement of loss of the Company's 20% interest in the MWT-BQE joint venture is presented as follows:

| | 3 months ended Sept. 30 | | 9 months ended Sept. 30 | |
|-----------------------------------|-------------------------|------|-------------------------|------|
| | 2018 | 2017 | 2018 | 2017 |
| | \$ | \$ | \$ | \$ |
| Revenue | - | - | - | - |
| General and administration | 10,234 | - | 28,746 | - |
| Net loss for the period | (10,234) | - | (28,746) | - |
| Other comprehensive loss | (21,820) | - | (8,294) | - |
| Comprehensive loss for the period | (32,054) | - | (37,040) | - |

9. TRADE PAYABLE AND ACCRUED LIABILITIES

| | Sept. 30, 2018 | Dec. 31, 2017 |
|---|----------------|---------------|
| | \$ | \$ |
| Trade payable and accruals | 896,668 | 319,721 |
| Payroll liability | 461,212 | 305,859 |
| Payable to joint venture (note 6(c), note 8(b)) | 96,400 | 96,400 |
| Interest payable (note 11) | 90,258 | 59,180 |
| Value added tax payable | 165,455 | 2,639 |
| | 1,709,993 | 783,799 |

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10. SHARE-BASED PAYMENTS

The Company's recorded stock-based compensation for the three and nine months ended are comprised as follows:

| | 3 months ended Sept. 30 | | 9 months ended Sept. 30 | |
|----------------------------|-------------------------|---------------|-------------------------|---------------|
| | 2018 | 2017 | 2018 | 2017 |
| | \$ | \$ | \$ | \$ |
| Stock options (a) | 31,695 | - | 94,051 | 2,610 |
| Deferred share units (b) | 5,165 | 33,523 | 6,779 | 39,354 |
| Restricted share units (c) | 63 | 953 | 201 | 1,118 |
| | <u>36,923</u> | <u>34,476</u> | <u>101,031</u> | <u>43,082</u> |

a. Stock options

Under the Company's Stock Option Plan (the "Plan"), the maximum number of shares reserved for exercise of all options granted by the Company may not exceed 10% of the Company's shares issued and outstanding at the time the options are granted. The exercise price of each option granted under the Plan is determined at the discretion of the Board at no less than the five-day volume weighted average share price preceding the grant date. Options granted under the Plan expire no later than the fifth anniversary of the date the options were granted and vesting provisions for issued options are determined at the discretion of the Board although the Company has a practice of having options vest over thirty-six months in equal installments.

Each vesting tranche in an award is considered a separate award with its own vesting period and grant date fair value. Fair value of each tranche is measured at the grant date using the Black-Scholes option pricing model. Compensation expense is recognized over the tranche's vesting period by increasing contributed surplus based on the number of awards expected to vest. The number of awards expected to vest is reviewed at least annually, with any impact being recognized immediately. Movements in the number of share options outstanding and their related weighted average exercise prices are as follows:

| | 2018 | | 2017 | |
|-----------------------------|---------------------------------|-------------------|---------------------------------|-------------------|
| | Weighted average exercise price | Number of options | Weighted average exercise price | Number of options |
| | \$ | | \$ | |
| Outstanding at January 1 | 0.07 | 7,133,333 | 0.11 | 4,333,333 |
| Granted | - | - | - | - |
| Forfeited | 0.07 | (400,000) | - | - |
| Expired | 0.15 | (533,333) | 0.19 | (600,000) |
| Outstanding at September 30 | <u>0.06</u> | <u>6,200,000</u> | <u>0.10</u> | <u>3,733,333</u> |
| Exercisable at September 30 | <u>0.07</u> | <u>2,000,000</u> | <u>0.10</u> | <u>3,733,333</u> |

The Company uses the Black-Scholes option pricing model in determining the fair value of the stock options. The following summary provides information on the grants and inputs to the Black-Scholes model.

On December 7, 2017, the Company granted 4,200,000 options with an exercise price of \$0.06 to the directors and employees of the Company. These options have a term of five years from the grant date and vest over three years with one-third vesting each year on the anniversary of the grant date. The fair value of these options determined using the Black-Scholes valuation model was \$0.05 per option. The significant assumptions in the valuation model were: volatility of approximately 119.19%, an expected option life of five years and an annual risk-free interest rate of 1.65%.

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| Exercise price range \$ | Weighted average remaining life (months) | Sept. 30, 2018 number of outstanding share options |
|----------------------------|---|--|
| 0.06 | 51 | 4,200,000 |
| 0.07 | 7 | 2,000,000 |
| 0.06 to 0.07 | 37 | 6,200,000 |

b. Deferred share unit

The Company implemented a deferred share units (“DSU”) plan, effective July 1, 2010, pursuant to which DSUs may be granted to management and non-employee members of the Board of Directors on an annual basis. Effective from October 1, 2013, the DSU Plan was amended to include certain senior managers of the Company.

The number of DSUs granted to a participant is calculated by dividing (i) a specified dollar amount of the participant’s compensation amount paid in DSU in lieu of cash, and by (ii) the five-day volume weighted average trading price of the shares of the Company traded through the facilities of the Toronto Venture Exchange on the trading days immediately preceding the date of grant. Dividends paid on the shares of the Company are credited as additional DSUs. Each DSU entitles the holder to receive a cash payment equal to the five-day volume weighted average trading price of the shares preceding the date of redemption. The DSUs vest immediately upon issuance and may only be redeemed within the period beginning on the date a holder ceases to be a participant under the plan and ending on December 31 of the following calendar year.

As the Company is required to settle this award in cash, it records these awards as a liability and a corresponding charge including changes to the fair value to stock-based compensation expense. The DSU is a financial instrument that is fair valued at each reporting date based on the five-day volume weighted average price of the Company’s common shares.

The following table presents the changes to the DSU plan:

| | Number of units | Value \$ |
|-----------------------------|-----------------|-------------|
| Balance, January 1, 2017 | 2,915,075 | 125,348 |
| Redeemed | (410,614) | (24,751) |
| Fair value adjustment | - | 55,932 |
| Balance, December 31, 2017 | 2,504,461 | 156,529 |
| Redeemed | (965,699) | (61,288) |
| Fair value adjustment | - | 6,779 |
| Balance, September 30, 2018 | 1,538,762 | 102,020 |

c. Restricted share units

The Company implemented a restricted share units (“RSU”) plan, effective August 5, 2010, pursuant to which RSUs may be granted to the officers of the Company. Under this plan, notional RSUs are granted and vested annually over a three-year term in general or otherwise determined by the Board. Upon vesting, the Company will settle the RSU in cash, having payment equal to the five-day volume weighted average trading price of the number of RSUs held preceding the date of redemption. RSU granted are accounted for and fair valued using the same methodology as DSUs.

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The following table presents the changes to the RSU plan:

| | Number of units | Value \$ |
|-----------------------------|-----------------|-------------|
| Balance, January 1, 2017 | 82,841 | 3,562 |
| Redeemed | (29,948) | (1,805) |
| Fair value adjustment | - | 1,549 |
| Balance, December 31, 2017 | 52,893 | 3,306 |
| Redeemed | - | - |
| Fair value adjustment | - | 201 |
| Balance, September 30, 2018 | 52,893 | 3,507 |

11. LOANS

| | Sept. 30, 2018 \$ | Dec. 31, 2017 \$ |
|------------------------|----------------------|---------------------|
| Employee loans (a) | 275,525 | - |
| Related party loan (b) | 47,100 | - |
| Convertible loans (c) | 1,500,000 | 1,497,726 |
| | 1,822,625 | 1,497,726 |

a. Employee loans

On May 16, 2018, the Company entered into loan agreements with multiple lenders, which include management and employees of the Company. The lenders have agreed to advance from various currencies with an aggregate principle amount of \$276,205. Under the agreement, the Company should repay the principle amount within 30 days following the receipt of the dividend from JCC-BQE. The loans will continue to bears interest at a rate of 12% per annum, and interest being payable monthly until maturity. The carrying amount of the employee loans on September 30, 2018 is \$275,525.

b. Related party loan

On June 16, 2018, the Company entered into a 6-month loan agreement with the Company's joint venture MWT-BQE. Under the agreement, MWT-BQE agreed to advance an aggregate principle amount of \$250,000 RMB, which bears interest at a rate of 8% per annum, and interest being payable upon maturity on Dec 15, 2018. The carrying amount of the related party loan on September 30, 2018 is \$47,100.

c. Convertible loans

On July 6, 2016, the Company entered into an 18-month convertible loan agreement with multiple lenders, which include certain directors, management, employees of the Company, individual investors and non-management insiders of the Company. The lenders agreed to advance a secured convertible loans with an aggregate principle amount of \$1,500,000. The Company grants to the lenders a security interest of all the personal property in which the Company now has or hereafter acquires. Out of the aggregate principle, \$1,441,000 are from single tranche lenders and the remaining \$59,000 are from multi-tranche lenders. Single tranche lenders agreed to advance the loans on the issuance date. Multi-tranche lenders agreed to advance funds to the Company in nine equal monthly tranches starting July 31, 2016 to March 31, 2017.

Under the agreement, the convertible loans bears interest at a rate of 8% per annum, and interest being payable semi-annually. The convertible loans are due for repayment 18 months from the effective date at their nominal value of \$1,500,000 or conversion into common shares of the Company at the holder's option with the conversion price of \$0.06 per share. Any unpaid and accrued interest that is to be converted into common shares shall be equal to the greater of \$0.06 or the market

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price on the date such interest becomes due and payable. At any time, the Company may elect to repay all or any portion of the principle and unpaid accrued interest prior to the maturity date.

On January 6, 2017, July 6 2017 and January 6, 2018, the Company paid out the semi-annual accrued interest in full to all the lenders.

The fair value of the liability component is calculated using a market interest rate for comparable companies of 15% for an equivalent, non-convertible secured loan at the date of issue. The residual amount, representing the value of the equity conversion component, is included in shareholders' equity as an equity component of the convertible loans. Transaction costs associated with the issuance of the convertible loans are allocated to the liability and equity components in its allocated proportion.

On January 5, 2018, the Company replaced the original convertible loans with replacement loans which extends the maturity date for another 12 months, from January 6, 2018 to January 6, 2019. The replacement loans have the same terms and conditions as the original convertible loans. The liability component has been reclassified from non-current liability to current liability as the convertible loan is due within 12 months of the reporting date.

The carrying amount of the liability component of the convertible loan and the interest payable are derived as follows:

| | Sept. 30, 2018 | Dec. 31, 2017 |
|---|----------------|---------------|
| | \$ | \$ |
| Face value of convertible loan issued | 1,500,000 | 1,500,000 |
| Less: amounts receivable from lenders | - | - |
| Transaction costs | (23,652) | (23,652) |
| Equity conversion component on initial recognition | (124,261) | (124,261) |
| Liability component on initial recognition | 1,352,087 | 1,352,087 |
| Accumulated interest and accretion expense since inception | 413,812 | 322,371 |
| Repayment of interest | (178,118) | (117,552) |
| Total liability component as at period end | 1,587,781 | 1,556,906 |
| Current interest payable included in accrued liabilities (note 9) | (87,781) | (59,180) |
| Convertible loans as at period end | 1,500,000 | 1,497,726 |

12. SHARE CAPITAL

Authorized: unlimited common shares without par value.

As at September 30, 2018 and December 31, 2017, the Company has 93,966,672 common shares outstanding.

13. INCOME TAXES

The income tax charge is a result of profits and withholding tax in two jurisdictions which are taxable and cannot be offset by accumulated tax benefits in other jurisdictions. Income tax expense is recognized based on management's best estimate of the weighted average annual income tax rate expected for the full financial year. The estimated average annual tax rate used for the three month period ended September 30, 2018 was 26% (26% at December 31, 2017).

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14. SUPPLEMENTAL CASH FLOW INFORMATION

Supplemental cash flow information (included within operating activities) is as follows:

| | 6 months ended Sept. 30 | |
|--|-------------------------|-----------|
| | 2018 | 2017 |
| | \$ | \$ |
| Change in non-cash working capital items | | |
| Increase in trade receivables | (1,531,826) | (173,363) |
| Decrease in inventory and work in progress | - | 20,137 |
| (Increase) decrease in other assets | (11,140) | 8,173 |
| Increase in accounts payable and accrued liabilities | 846,038 | 17,957 |
| Increase in deferred revenue | 94,479 | 8,239 |
| | | |
| Change in non-cash working capital items | (602,449) | (118,857) |

15. COMMITMENTS

The Company has commitments of \$568,449 under operating leases for office and laboratory premises, for laboratory assay services, and for office equipment, as follows:

| | \$ |
|------|---------|
| 2018 | 67,552 |
| 2019 | 187,738 |
| 2020 | 189,269 |
| 2021 | 63,606 |
| 2022 | 60,284 |
| | |
| | 568,449 |

16. REVENUE

The Company adopted IFRS 15 effective January 1, 2018.

The Company is focusing on monetizing the value of its IP and expertise primarily through the service of long-term operation and maintenance of water treatment plants which generate recurring revenue that is directly linked to plant performance. As the period between the identification of new projects and treatment plants entering their operation phase can be lengthy, the Company also generates revenue from technical services relating to water management that are project specific and generally non-recurring in nature. The two main streams of revenue of the Company are: (1) Operation and maintenance of water treatment plants, and (2) Technical services relating to water management, which include process consulting, laboratory treatability assessments, field pilot demonstrations and feasibility engineering studies. The Company functions as operators of water treatment plants and as providers of technical services relating to water management.

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The Company's revenue streams are as follows:

| | 3 months ended Sept. 30 | | 9 months ended Sept. 30 | |
|----------------------------------|-------------------------|------------------|-------------------------|------------------|
| | 2018 | 2017 | 2018 | 2017 |
| | \$ | \$ | \$ | \$ |
| Water treatment plant operations | 912,367 | 1,000,049 | 986,696 | 1,153,150 |
| Technical services | 980,810 | 578,278 | 1,973,722 | 2,046,054 |
| | <u>1,893,177</u> | <u>1,578,327</u> | <u>2,960,418</u> | <u>3,199,204</u> |

17. SEGMENTED INFORMATION**a) Geographic information**

The Company mainly generates revenue from Canada (country of domicile) and occasionally from foreign regions. The Company's revenue by geographic locations, presented based on the location in which the sale originated from, are as follows:

| | 3 months ended Sept. 30 | | 9 months ended Sept. 30 | |
|---------------|-------------------------|------------------|-------------------------|------------------|
| | 2018 | 2017 | 2018 | 2017 |
| | \$ | \$ | \$ | \$ |
| Canada | 1,548,549 | 1,159,108 | 2,290,118 | 2,031,862 |
| Latin America | 235,818 | 348,122 | 466,666 | 937,933 |
| USA | 71,024 | 45,816 | 158,068 | 167,224 |
| Other | 37,786 | 25,281 | 45,566 | 62,185 |
| | <u>1,893,177</u> | <u>1,578,327</u> | <u>2,960,418</u> | <u>3,199,204</u> |

The Company's non-current assets, excluding non-current deposits, by location of assets are as follows:

| | Sept. 30, 2018 | Dec. 31, 2017 |
|--------|------------------|------------------|
| | \$ | \$ |
| Canada | 50,573 | 42,463 |
| China | 6,074,948 | 5,095,256 |
| | <u>6,125,521</u> | <u>5,137,719</u> |

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b) Information about major customers

The following table presents revenue from individual customers exceeding 10% of total revenue for the three and nine months ended September 30, 2018 and 2017.

| | 3 months ended Sept. 30 | | 9 months ended Sept. 30 | |
|-------------------------------|-------------------------|------------------|-------------------------|------------------|
| | 2018 | 2017 | 2018 | 2017 |
| | \$ | \$ | \$ | \$ |
| Customer A | 912,367 | 1,000,049 | 986,696 | 1,153,148 |
| Customer B | - | 236,251 | - | 292,751 |
| Customer E | - | 56,218 | - | 293,317 |
| Customer F | - | - | 277,407 | - |
| Customer G | 132,326 | 63,549 | 352,951 | 489,239 |
| Customer H | 194,850 | - | 256,950 | - |
| | <u>1,239,543</u> | <u>1,356,067</u> | <u>1,874,004</u> | <u>2,228,455</u> |
| Percentage from total revenue | 65% | 86% | 63% | 70% |